German EU policy post-Merkel: Greener but still no big spender

- **All eyes on the next government’s EU fiscal stance.** The Greens are advocating looser debt rules and turning the NGEU into a permanent fiscal capacity. However, in the two most plausible coalition scenarios, the Greens have to find common ground with either the Conservatives (black-green coalition) or the Liberals (traffic light coalition). Both call for re-instating the debt rules in the post-pandemic world and emphasize the one-off nature of the NGEU. Thus, we do not expect any significant shift of Germany’s EU fiscal policies. The odds of an election surprise contributing to a stronger EUR remain low. The autumn debate about the reform of the SGP will be the first proof of this new/old fiscal stance.

- **Putting the Green Deal to work: Germany role-modelling green transformation at measured pace.** The next German government is very likely to support the extension of the EU’s Emission Trading System to additional sectors, as already pioneered nationally. Further looming legislative actions (e.g. end of free allowances for energy-intensive sectors once the CBAM is introduced) will face more resistance given Germany’s strong industrial base. As the Greens do not firmly believe in the “invisible green hand of markets” (i.e. price signals), they are likely to also push for stricter regulation and an active green industrial policy (on the national and EU level). All in all, we expect Germany to role-model and lobby for a green transformation that resembles more an evolution than a revolution.

- **Germany to remain in the free-trade camp, but less of a driving force.** By virtue of its economic weight and openness, Germany is always going to be instrumental in shaping the EU’s foreign and trade policies. However, these policy issues might shift a bit to the back burner, at least until the next chancellor has gained in political weight, at the EU and global level. As the Greens insist on linking any future trade/investment deals with social and environmental standards and are relatively hawkish on China, we do not expect any progress with respect to pending deals (e.g. the frozen CAI).

- **No push for ambitious EU institutional reform: Neither by Laschet nor Baerbock.** A more coherent policy approach and institutional reform are indispensable given EU-27 heterogeneity, global geo-economic rivalry and mounting challenges such as climate change or migration. With treaty changes out of reach given lack of support in the EU-27, fostering coalitions of the willing or a switch to qualified majority voting in more policy fields seem to be the max either candidate could aim for. There is little incentive for any candidate to portray him/herself as a pro-European visionary, as such a stance does not pay off at home. Thus, no strong German push to advance the EU’s role as a geopolitical player is to be expected.
Focus on implementation given the stuttering German-French engine

2020 has shown that the EU rule of thumb – institutional progress mostly happens in crisis times – is still holding. Chancellor Merkel leveraged her role as the EU’s most experienced crisis manager, finalizing key initiatives during the German EU presidency in H2: (i) The Multiannual Financial Framework 2021-2027 with the Green Deal and the EUR 750bn NGEU fund has been agreed upon. Though implementation will keep EU institutions and members busy, looming conflicts included. (ii) The ESM was reformed to act as a backstop to the SRF. (iii) The Brexit deal was signed at the eleventh hour with gaps in the treaty still to be filled.

What will dominate the EU policy agenda over the next four years? In our view, the focus will be on the implementation of already agreed projects, rather than another leap forward in EU integration (unless another crisis hits). The European electoral calendar will likely also curtail more ambitious initiatives. France – which holds the EU presidency in H1 2022 – is facing presidential elections in May 2022 at a time when the new German government will just have assumed office. At least initially Germany’s contribution to shaping EU policy could be smaller than in the past few decades, until the next German chancellor has gained in European and global political weight. Thus, Europe might be lacking strong leadership for most of next year.

Still, in several policy areas the composition of the next German government and the role of the Greens in particular could make a difference. The below timeline visualizes these important upcoming milestones such as tax-related legislation for new own resources, the reform of the SGP, putting the EU Green Deal to work and improving the efficiency of the EU’s foreign and security policy. In this report we first provide a concise overview of the parties’ positions with respect to key European policy areas. We then sketch which impulses we expect from the next German government based on the most plausible coalition options.

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1 36% of the population expects Germany’s influence to be weaker in a post-Merkel era according to a survey by the Körber Stiftung.
EU foreign & trade policies: Struggling to manage trade-offs in a less cooperative world

The EU is facing a delicate balancing act of (1) strengthening its “open strategic autonomy” while at the same time (2) enhancing multilateralism and (3) partnering with both, the US and China, to address key global challenges like climate change, terrorism and corporate tax avoidance. The recent freezing of the investment agreement with China (CAI) and the inability of the member states to agree on a common post-pandemic trade strategy in May in Porto serve as a reminder of how paralyzing the global backdrop can be. The strategic and systemic rivalry between China and the US is mainly fought in the geo-economic arena and industrial policy is becoming more dominant globally (US Strategic competition act of 2021). Thus, it will be increasingly difficult for the EU (and Germany) to separate trade and investment policies from foreign policy.

Trade/investment policy – remaining in the free-trade camp? The EU is set to remain a champion for multilateralism with the single market being its biggest asset. But it will at the same time further expand its armory of economic weapons (e.g. the recently proposed legislation on foreign subsidies). There is general consensus on the reduction of asymmetric dependencies, especially with respect to critical raw materials, active pharmaceutical ingredients, semiconductors and cloud computing (see May update of the EU New Industrial Strategy). But as some member states are more inclined to resort to more protectionism in general, it will be key whether Germany remains a vocal supporter of free-trade. With the UK gone, Germany (the Nordics and Netherlands) lost a free-market proponent, tilting the balance towards members more inclined to state interventionism. While all parties (apart from the Left) advocate enhanced multilateralism and “fair” competition, only the Conservatives and Liberals call for reviving efforts to realize a transatlantic free-trade zone. The Greens and the Social Democrats insist on linking free-trade agreements with environmental and social standards thereby risking to complicate progress in trade talks further.

Foreign/defense – German-French vanguard. The US security umbrella will remain indispensable in guaranteeing the EU’s security, despite the fact that the EU’s defense capabilities have been somewhat strengthened. All German parties (apart from the Left) are strongly committed to NATO. The Greens, however, reject the “static” 2% of GDP defense spending target and call for linking expenses to tasks attributed to members (e.g. a cyber defense center). With respect to foreign policy, national and union-wide policies will continue to coexist for the foreseeable future, leading to “lowest-common-denominator policies” (Economist, Oct 2020). The debate about qualified majority voting in foreign and security policy is likely to resurface – with all German parties in favour of it and confident of implementing it until 2025. However, as recent attempts to move in that direction have all failed, the “coalition of the willing” format is the only realistic tool to be used in case a union-wide consensus is not attainable (e.g. Normandy Format like in the Ukraine/Russia peace process). As long as the 27 members decide on foreign and security policy issues by unanimity, the EU’s role as a geopolitical player is not expected to advance markedly.

Views on strategic sovereignty – same but different: While all German parties are in favour of strengthening Europe’s “capacity to act”, they differ in terms of the desired degree of sovereignty to relinquish and the preferred toolboxes to achieve it. The Greens advocate a stop of the Nord Stream 2 pipeline to reduce energy dependence on Russia. The Social democrats are in favour of the protection of “key industries”, while the Conservatives call for a more “proactive” foreign policy.

Relationship with the US under Biden. Apart from healing deep domestic divisions,
the Biden administration is focused on shoring up alliances with like-minded partners. However, rebooting the transatlantic relationship does not seem to be a primary goal in itself for the new administration, as the US focus is increasingly geared towards Asia-Pacific. All German parties (apart from the Left) aim for reviving the transatlantic partnership, though the Greens tend to put intra-EU relations first. In addition, differences with respect to the parties’ stance on China might come to the fore here.

**Germany instrumental in shaping the EU-China strategy.** EU-China relations are under considerable flux. All German mainstream parties echo the EU’s labelling of China as “a partner, competitor and systemic rival” (see 2019 EU ‘Strategic Outlook’). Given China’s lucrative domestic market, economic interdependencies in terms of trade and investment are likely to grow. The turnover of German foreign subsidiaries in China has almost tripled from EUR 74bn in 2010 to EUR 194bn in 2018 (see Figure 4). As its trade and investment dependencies are strongest in the EU, Germany is likely to play an active role in shaping the future relationship with China (see Figure 6). Laschet’s approach towards the Asian superpower seems to very much resemble the “steady as we go” policies of Angela Merkel, as exemplified by his recent reply to Biden’s China stance “Do we need another adversary?” (FT interview, June 21). The Greens, however, are far more hawkish on China, more inclined to mix trade and investment policies with foreign policy. Thus, we do not expect the unfreezing of the Comprehensive Investment Agreement with China to be among the top priorities of a likely black-green government.

**EU-UK relations to be marred by continued tensions.** On April 28 the EP ratified the post-Brexit EU-UK trade and cooperation agreement which is the most comprehensive agreement ever concluded between the EU and a third country (and might serve as a blueprint for binding neighbouring countries closer to the EU). Still, the UK and EU will continue talks over the next years to fill gaps in the treaty, including the area of financial services. Keeping up EU standards as a precondition for access to the single market remains crucial, though, based only on equivalence assessments. The recent adoption of adequacy decisions for the UK means that e.g. private data can flow freely, at least over the course of the next four years. Generally, there seems to be a relatively high risk of regulatory divergence, which will be subject to future scrutiny by the Commission. It remains to be seen whether the level playing field is working with the final review due only in four years’ time. With respect to foreign and security policy (not forming part of the Brexit agreement) most of the German parties call for a close alliance with the UK.

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2 Carnegie, Working with the Biden administration – opportunities for the EU, January 2021
3 Andrew Duff, Europe after the Brits, EPC March 2021
EMU – many unresolved issues

NGEU – nucleus for a permanent fiscal capacity? In June, the EU Council greenlighted the first disbursements of the EUR 750bn Next Generation EU funds (NGEU) based on EU COM’s assessment of national recovery and resilience plans. Despite the focus on recovery from the pandemic, climate change and digital transformation, member states were allowed to follow “a broad concept of investment as capital formation” (EU COM 2020). Thus, NGEU is less of a counter-cyclical crisis tool but rather an intra-EU debt-financed redistribution vehicle with a loose link to facilitate national investment. Still, it is sometimes considered a nucleus for the long-discussed fiscal capacity to mitigate external shocks in the euro area and also to improve convergence within the EU via higher investment. Member states like France, Spain and Italy as well as the ECB call for making it a permanent facility with additional funding. For Germany, the NGEU marks a fundamental change of course in EU policy. However, the approval of the Conservatives’ in the Bundestag was only secured on the assumption of the NGEU being a one-off project.1 The Conservatives (and the Liberals) are sticking to that position, while the Greens and the SPD are in favour of turning the NGEU into a permanent facility as part of the EU budget. Under the current institutional framework of the EU such an initiative would require unanimity – too high a hurdle even with a new German government being potentially more accommodative. The success of the NGEU will determine whether the net contributors to the EU budget will be willing to consider a permanent mechanism, i.e. whether common debt financing has resulted in more economic resilience of receiving member states. In any case, decisions on that matter will fall beyond the next German government’s term.

Providing the EU with new own resources faces a reality check. The funds borrowed for the NGEU are to be repaid from 2028 to 2058 with new EU own resources. EP and Council agreed to introduce new taxes over the next seven years: a digital levy, an own resource based on the European Emission Trading System, a Carbon Border Adjustment Mechanism (CBAM) and possibly a financial transaction tax and an own resource based on corporate taxes. For several reasons this is a highly ambitious proposal (see FE, Aug 4): (i) Some of the new own resources have complex links to international negotiations (digital levy, see Figure 10). (ii) Some of them like the CBAM might have a negative impact on trade relations as already threatened by the US and China. (iii) Each new tax needs a separate implementation legislation – subject to an unanimous vote of the EU-27. Beyond last year’s political agreement, there is no consensus among members on allocating the EU COM with the competence of tax collection as another step towards a true fiscal union. If the COM’s roadmap holds (see Figure 11), it will be up to the next German government to decide on Germany’s stance. So far, Germany has been one of the countries reluctant to allocate more tax competences to the EU. It will likely stick to this position if ruled by a CDU/CSU-led government – even with a Green partner. The Greens or the SPD advocate conceding more rights to the COM to introduce and collect new revenues for the budget – not least to fund additional EU investment.

Review of the fiscal framework: Buying time. Stimulus-induced higher fiscal deficits are likely to further fuel the debate on SGP reform (FE March 1). Current fiscal rules have been criticized for being too complex and inducing pro-cyclicality. There are two lines of arguments here how to deal with new debt levels in the EA (2020: 100% of GDP): One camp is concerned that some countries have exceeded fiscal targets too far to ever be

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1 The German Constitutional Court rejected a preliminary injunction against the EU recovery package in April but accepted the complaint and will look into the arguments in the principal proceedings.
able to comply with them again. The other camp argues that low-for-longer interest rates and the improved debt sustainability are here to stay. In addition, there has been no decision so far on how to account for the debt accumulated through the NGEU (EU level vs. national debt) and how this impacts national debt trajectories.5 The discussion will heat up in H2 2021 when the COM is to present its proposal – likely based on last year’s work of the European Fiscal Board which includes an expenditure rule and a country-specific debt anchor. Member states are split along the same fault lines as within Germany: The Conservatives and Liberals are strongly in favour of the current fiscal rules and their (perceived) strict compliance (“stability not debt union”). The centre-left parties, incl. the Greens, however, call for rules that prevent austerity and provide (even) more flexibility. As it will take time to find common ground, ECOFIN will in the meantime extend the suspension of the general escape clause of the SGP to 2022 as well.6

Turning the ESM into a true EMF – not yet. This idea has been floated some time ago and forms part of the COM’s roadmap to a full EMU. While all major parties are supportive of it in general, they actually mean different things. The Greens back unconditional credit lines for member states and want to integrate the ESM/EMF into the institutional set-up of the EU to strengthen its democratic legitimation. The Liberals regard it as an independent body for stricter fiscal control and, like the SPD, want to establish a sovereign debt restructuring mechanism. The CDU/CSU only vaguely mentions the ESM in the context of the Banking Union. In our view, further reform progress is rather unlikely to happen in the near future as the current reform of the ESM has just been approved.7

The long road of completing banking and capital markets union. For the CMU to be completed a long list of outstanding initiatives needs to be pushed forward, e.g. the harmonisation of (corporate) insolvency rules, enhancing the single rulebook for capital markets or simplifying rules for listing of public companies. The details of these initiatives will keep experts busy for some time, further delaying the positive impact for Europe’s corporate sector. Election manifestos are lacking details on most of the issues, apart from the most contentious leftover of the BU, the European Deposit Insurance Scheme (EDIS). All parties agree on an EDIS as a tool for better risk sharing, but they differ on how to get there. The FDP, the Conservatives and, to a lesser extent, the SPD insist on a reduction of risks on banks’ balance sheets as a precondition (e.g. divestment of NPLs and/ or limiting banks’ domestic sovereign exposure, see FG April 9). The Greens, however, are taking a more accommodating stance in the current discussions at the EU level. The COM is set to present a new roadmap for the December summit to overcome the current deadlock.

5 The Bundesbank calls for EU debt to be counted as national debt and deficits whereas Bruegel argues that this would be counterproductive for the required fiscal stance for a broad recovery.
6 Following the ECOFIN meeting in May, Executive Vice-President Dombrovskis said “… we can confirm our approach that we would keep the general escape clause activated in 2022 but no longer as of 2023”.
7 Abiding by a request of the German Constitutional Court, the German president will not sign the ratification of the ESM into law. This follows an emergency motion by a group of FDP MPs.
EU climate policies: The cost of decarbonisation to move center stage

EU climate policies received strong impetus with the provisional agreement on the European climate law reached on April 21 (to be formally approved by Parliament and Council). It aims to reduce EU-wide GHG emissions by at least 55 per cent in 2030 relative to 1990 levels, and to achieve net zero GHG emissions in 2050. As climate policy is an intersecting policy area, it cannot be assessed in isolation. The interaction with a multitude of policies and layers (trade/competition/foreign/innovation and social policy) from national to EU to global level further complicates the assessment. An upcoming milestone is the EU’s roll-out of 13 policy proposals as part of its “Fit for 55 package” to be released on July 14th:

- **ETS expansion.** The Commission is likely to propose to revise and expand the scope of the EU ETS to shipping, road transport and heating fuels in a parallel system. How to mitigate the distributional aspects of this extension will be a hotly debated issue. While Germany, Denmark and Sweden support the extension, backlash from poorer CEE member states is expected. The German National ETS, which started at the beginning of this year with a de facto tax of EUR 25 per ton of carbon on heating oil and gas, petrol and diesel is likely to serve as a role model. A qualified majority of member states and MEPs has to vote in favour of the ETS revamp.

- **CBAM: An untested instrument to avoid carbon leakage and be a source of income.** As the introduction of a CBAM is unchartered territory at the national level, it is likely to start with limited scope (see leaked draft proposal). The carbon border tax is designed to impose levies on imports from countries without equivalent carbon price mechanisms. Amending the EU Emission Trading System directive to include importers, could theoretically occur with a qualified majority of Member States. However, as the EU and US have very different climate philosophies and WTO-compliance remains an issue, lack of political buy-in might prevent a fast and wide-ranging introduction of a CBAM.

- **Global climate club with minimum CO₂ price:** As unilateral EU action might trigger retaliation from trading partners, the idea of a global climate club has been forwarded by think tanks and advisory bodies as the only viable solution. For such a club to be successful agreement on a global minimum price, its dynamic adjustment and the covered industries would be necessary. While all of that still sounds like wishful thinking, at the corporate level, the number of companies which have already or plan to use an internal carbon price has risen to 2,000 globally (CDP).

- **Green tech race has started:** Given the scale of the needed economic transition to a net-zero world, calls for a European green industrial policy have become louder. In its new industrial strategy existing instruments like Horizon Europe, the European Semester or European Alliances (on batteries and clean hydrogen) are mentioned. Shortening innovation cycles (especially in the deployment and diffusion phase) will be key in order to win the global Green tech race. US Secretary of Energy Granholm said the development of cleaner energy technologies would unlock a “USD 23tn market” by 2030 (FT, April 21). In the end, it will boil down to the question whether there is demand for (non-subsidized) green products, which can be fostered via EU certification etc. The Greens are the only party openly advocating the promotion of key sectors for the green transformation.

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8 CRF, How to decarbonise EU road transport?
EU is advancing its aspiration as global digital regulator and further deepening the digital single market

The EU (still) is the world’s largest exporter of services, but in a post-pandemic world services will be increasingly delivered digitally (see Figure 17). Thus, promoting the free flow of data on the one hand and ensuring fair competition, digital sovereignty and setting regulatory standards on the other hand, are set to remain high on the EU’s agenda. Over the past couple of years, the EU has advanced the digital single market with a series of regulations9 and its status as “regulatory” superpower by exporting its digital rules. Setting global data protection standards (outside of China) with the GDPR in 2018 has been the most prominent example. Now, the main challenge will be to find the right balance between digital sovereignty/ protection of citizens’ rights and not sacrificing the benefits of an open digital economy:

- **Digital single market**: Fair competition and the containment of market power of dominant Tech players, in particular, will remain in focus. The Commission proposed two important new rulebooks in December 2020. The [Digital Markets Act](https://eur-lex.europa.eu) (DMA) will impose new obligations on so-called gatekeepers. It is departing from the concept of abuse and allows sector-wide investigations to prevent anti-competitive actions. The [Digital Services Act](https://eur-lex.europa.eu) (DSA) is drafted to limit spread of illegal content and goods. While all German parties voice support for the two rulebooks as minimum standards, the DMA recently faced criticism from the current government of Germany, France and the Netherlands, who are calling for stricter rules. Given EU infighting it might only be enacted early next year.

- The EU is also progressing in setting standards with its [human-centric approach to AI](https://eur-lex.europa.eu). This first-ever legal framework is an example of the EU’s “regulate-first” approach, which is not undisputed as the [OECD](https://www.oecd.org) is also in the midst of creating a consensus on AI. All parties (implicitly) subscribe to this “AI made in Europe” approach, whereas the SPD puts social aspects first.

- **Digital sovereignty**: One of the priorities of the VdL-Commission is Tech Sovereignty. 20% of the Recovery and Resilience Facility are earmarked to be spent on critical technologies and infrastructure related to AI, microprocessors, 5G networks, the Gaia-X cloud initiative, quantum computing and cybersecurity. All German parties agree on aiming for a higher degree of Tech sovereignty, especially with respect to critical infrastructure on the national and EU level.

- **Cross-border data flows** between the US and Europe are the largest in the world. Currently they account for over half of Europe’s data flows and about half of US data flows ([Bitkom](https://www.bitkom.org)). One year after the invalidation of the EU-US privacy shield (applying to personal data only), there seems to be not much progress towards a new legal basis compliant with the CJEU judgement. Multilateral rules on digital trade will be discussed on the upcoming WTO meeting in Geneva in November (JSI trade-related aspects of e-commerce). But also on a regional level, a new generation of digital trade agreements has emerged ([CPTPP, DEA, DEPA](https://eur-lex.europa.eu)).10 The Liberals and the CDU will be more inclined to push bi- and multilateral trade agreements.

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9 Free flow of data regulation in 2018, etc.
10 Strategic choices for the EU’s digital trade policy after the US election, Jacques Delors Center
Migration is back: EU policy hinging on national approaches

Common Asylum and Migration Policy – more conflicts than achievements. Migration is likely to reappear on the EU agenda and citizens’ minds. Refugee and immigration policy are still very much in the hands of the member states despite very good reasons to agree on a joint approach. The “EU-Turkey Deal” from 2016 (similar agreements exist between Italy – Libya and Spain – Morocco) was successful only at first glance as many issues remain unresolved: (1) The deals render the EU vulnerable to blackmailing by (non-democratic) states as recent incidents on the Turkish or Moroccan border have shown. (2) It does not solve the fundamental problem of unequal burden sharing within the EU with Southern member states being most exposed (e.g. Greece, Italy), some member states voluntarily welcoming refugees (e.g. Germany and France) and others refusing to do so (e.g. Poland, Hungary, Slovakia, Austria, Denmark). (3) The deal risks damaging the EU credibility with respect to spearheading the defense of human rights.

New pact, old divisions. President von der Leyen declared a “fresh start in migration” as one key priority resulting in an almost 50% hike of resources earmarked for migration and border management in the 2021-2027 MFF. Furthermore, the Commission proposed a “New Pact on Migration and Asylum” last September. However, the pact largely sticks to the current policy course, focusing on reinforced external border controls and strengthened partnership with third countries. It includes a rather timid push towards more solidarity, allowing members to contribute to differing degrees (voluntarily reception of refugees, sending border guards or supporting repatriations). A binding redistribution mechanism should apply only in case of exceptional circumstances. As members cannot find common ground on the issue of redistribution, the long-standing blockade in the Council on refugee policy is likely to continue. So far, only an extension of the EU-Turkey deal is in the making (see Council decision, June 24). Some progress has also been made to better distinguish desired from unwanted migration. The Blue Card Directive was revised to attract more foreign talent given the aging European labor force.

Migration still a key issue (not only) for German voters. A common refugee policy tops the list of voters’ European policy priorities for the next federal government. Germany absorbs the largest number of refugees (e.g. about 25% of all first time applications in the EU in 2020). Thus, fairer burden sharing is a joint goal among the German political parties. On other aspects of refugee policy, though, there is a clear left-right divide: In line with the proposed EU pact, the Conservatives and Liberals support strong border controls and wish to continue migration deals with third countries. In addition, they want to prevent secondary migration (i.e. refugees registered in other member states moving to Germany), an issue they perceive as not sufficiently addressed at the EU level. The Conservatives even consider asylum decisions (and not only prescreening) being taken at EU run centers at the external border. In contrast, the SPD and Greens are generally skeptical about a “human” fortress Europe. They stress the individual right to seek asylum and the fact that some cities and municipalities are willing to voluntarily take in more refugees.
No real appetite for ambitious EU institutional reform

Tackling the “democratic deficit”. Institutional reforms are a sensitive topic in the EU, as member states scrutinize any proposed changes with regard to their impact on national sovereignty. The Lisbon Treaty in 2009 was the last major treaty change. Reforms might be needed now more than ever given increasing heterogeneity within the EU, geo-economic rivalry and mounting new challenges such as climate change. In her “Agenda for Europe” Commission President von der Leyen called for a more powerful EP with a full right of initiative and more policies subject to the co-decision procedure. She proposed a commitment of the Commission to respond with a legislative act, if requested by the EP with a majority of its MEPs – giving the EP a right of initiative. All major German mainstream parties are in favour of a stronger role of the EP. As the EP is currently more fragmented than ever and a new right-wing party formation is in the making, securing a cross-party majority for launching own initiatives is rather challenging. In addition, EU citizens would like to see action from the EP in areas where the EU itself has only limited competences.

Switching to qualified majority voting (QMV) in more policy areas looks likely. While QMV has become the norm in the EU’s decision making, in key policy areas (e.g. taxation, social and certain aspects of climate, energy) unanimity is still required. Achieving unanimity via compromises can be a key strength of the EU, but it can also lead to lengthy, fruitless or “lowest-common-denominator” outcomes. Changing from unanimity to QMV could be a fairly straightforward process when based on the so-called bridging clauses of Art. 48(7) TEU. In 2019 the Commission proposed a phasing in of QMV for tax policy (starting with tax evasion and climate-related taxes), but the ECOFIN remains split on such a move. All major German parties agree that a change of voting procedures is necessary to improve the EU’s capacity to act – however, the extent varies. The Greens want a complete switch to QMV, while the Conservatives want to limit the extension to foreign and security policy. The SPD supports a step-by-step introduction starting with fiscal, foreign and security policy.

Conference on the Future of Europe: Just a forum for reflection. After a promising start with treaty changes not off the limits, it now seems like the conference is less about the “finalité” of integration but about its purpose in general. Lengthy debates between the Council, the COM and the EP raised doubts about whether the outcome of the debate will be seriously considered by the member states at all. Any future German government, though, will constructively support the conference. All parties stressed the importance of including the perspective of citizens called for openness to treaty changes. The latter remains rather unlikely. Any progress in integration will stem from intergovernmental agreements or nonbinding “coalitions of the willing”.

Eurosceptics are still the exception in the political party landscape. Apart from the far-right AfD (scoring at around 10% currently), all mainstream parties are supportive of further EU integration. But they disagree on the degree of integration and handing over further competences to the supranational level. The Greens are most progressive, proposing the transition to a “European Federal Republic”. CDU and FDP advocate subsidiarity as the guiding principle. In the European Parliament, the EPP (CDU/CSU) still is the group with most seats, but the Greens/EFA (the Greens) are gaining in importance and now constitute the fourth strongest group. Institutional reforms have proved to be difficult in the past, and we doubt that the next German government will spend a lot of political capital on this matter.
**Greens’ influence in the next government will determine Germany’s EU stance, especially its preparedness to pay**

To be anchored in the EU and supportive of European integration forms part of Germany’s raison d’État. But Merkel’s departure will leave a void in EU leadership as it will take time until the new chancellor will have gained political weight at the EU and global level. While Merkel could focus her attention on European and international affairs during large parts of her terms, her successor might be more occupied with domestic politics and coalition management. Especially, since we are going to see a novelty coalition at the federal level. This also holds true for important ministers like the Finance Minister whose party background will likely play a role in the government-related discussions in the Eurogroup. All in all, the next German government will be clearly pro-European, striving for an active and constructive role within the EU, but only after the new coalition partners found common ground. Thus, the traditional German-French engine might be stuttering for a while. Even more so as France is facing elections and traditional alliances in certain policy fields have been weakening. While Germany’s EU policy narrative will not change significantly under the new leadership (see our analysis of the Conservatives’ and Greens election manifesto), the composition of the coalition will still matter:

**Conservative-green coalition – more pro-European talk but no major (fiscal) policy shift.** A black-green government led by Laschet (our current baseline) should remain strongly pro-European. By refusing to close the borders to Belgium and the Netherlands as North Rhine-Westphalia’s PM during the height of the pandemic, Laschet has held up the idea of European integration. He is a strong supporter of the German-Franco alliance and is likely to build on existing joint initiatives for providing leadership to and modernizing of the EU. He has demonstrated his ability to reconcile parties and develop common solutions, thus able to step in Merkel’s footsteps at the EU level in that respect. A CDU/CSU-led government will defend its (fiscally conservative) principles but also be flexible enough to take action when needed (with the agreement on the NGEU the most prominent proof of that). There is strong overlap with the Greens with respect to positioning the EU as global player as well as strengthening the EU in the global digital and green tech race. Key bones of contention will be foreign policy (especially Nord Stream 2), migration and scope and speed of the advancement of the euro area (incl. its social policy angle). Opposition might come more from Laschet’s party than himself – in particular on the latter where the GCC plays a role as well.

**Green-led traffic light coalition – more committed.** A Green-led government with chancellor Baerbock would start off by being more visionary and actively push for reforms, aiming to instrumentalize the single market for their target of social and ecological transformation. But being caught up in EU realpolitik soon, bold institutional reforms or the evolution of a social union with minimum wages and labour market institutions will remain unlikely. Common priorities among all three coalition partners will be the EU’s green and digital agenda though differences remain with respect to preferred instruments. As these priorities are shared with the European Parliament, this could lead to some new dynamics with the German Greens and the Green EP fraction in the driver’s seat. But with respect to further fiscal integration and transferring more sovereignty to the EU level, the Liberals will likely keep their coalition partners at bay.

**Conservative-liberal coalition—tighter fiscal reins.** As the Left party is polling fairly close to the 5% threshold, a conservative-liberal coalition (polling at 42%) is emerging as the fiscally most conservative tail risk. Both parties stick to their conviction that the SGP fiscal rules should be applied sooner rather than later in a post-pandemic EU and emphasize the one-off character of the NGEU. Thus, such an election outcome is likely
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to meet stronger skepticism by financial markets than the before mentioned options. Compromise on fiscal reforms and progress on the EU’s own resources will be challenging with such a government. Still, even the Merkel-led conservative-liberal government agreed on ESM and BU at the times of the debt crisis to stabilize the euro area.

**Bottom line: Odds of an election surprise contributing to a stronger EUR remain low**

The Greens are advocating looser debt rules and turning the NGEU into a permanent fiscal capacity and are likely to be the kingmakers for the next government coalition. In the two most plausible coalition scenarios, however, the Greens have to find common ground with either the Conservatives (black-green coalition) or the Liberals (traffic light coalition). Both are known for their fiscal orthodoxy, call for reinstating the debt rules in the post-pandemic world and emphasize the one-off nature of the NGEU. Thus, we do not expect any significant shift of Germany’s EU fiscal policy course. The odds of an election surprise contributing to a stronger EUR (via a green-left coalition) remain low. The autumn debate about the reform of the Stability and Growth Pact will be the first proof of this new/old fiscal stance of the next German government.

We would like to thank Ursula Walther and Jenny Franke for their valuable contributions to this report.
Appendix 1

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