

# LETTER FROM BERLIN



## Germany in Crisis

*As winter approaches, the governing coalition is being punished.*

BY KLAUS C. ENGELEN

**W**ith 10 percent inflation, a looming recession, and the threat of deindustrialization, Europe's largest and strongest economy is experiencing the worst erosion of the fundamentals of its prosperity since the post-war economic miracle in the 1950s and 1960s built Germany into an economic powerhouse.

As many of Germany's 84 million citizens contemplate the end of their prosperity, the ruling "traffic-light" coalition of Social Democrats, Greens, and Free Democrats is confronted with a mission impossible. As *Politico* summed up the crisis: "Two pillars of Germany's economic success story—cheap energy supplies from Russia and low security spending—collapsed this year."

No wonder a recent INSA opinion poll (*Meinungstrend*) confirms the frustration of German voters with their leaders. With only 44.5 percent approval between them, the three ruling parties of the coalition have lost their majority. Looking at recent opinion polls, the major opposition—the union of Christian Democrats and the Bavarian CSU that ignored the dependency on Putin's gas and oil—was leading the polls. With Friedrich Merz as its new leader, the CDU/CSU reached 27–29 percent, the SPD 18–20 percent, the Greens 17–22 percent, the right-wing AfD 13–16 percent, the FDP 5–7 percent, and the Linke 4–7 percent.

One reason for the eroding support for the coalition under Chancellor Olaf Scholz (SPD), who served as finance minister in Merkel's last

CDU/CSU-SPD coalition, was that not enough urgency and speed were brought to bear in the precious months after the Russian invasion of Ukraine in February to mobilize all the country's energy resources. The coalition also disregarded the ambitious climate transition demands by shutting down German nuclear reactors. Relief plans to help households and the business sector cope with exploding gas and electricity prices were delayed, especially by the Green party.

A case in point was the surcharge levy plan proposed by Minister for Economic Affairs and Climate Action Robert Habeck from the Greens. Under this plan, consumers in Germany would take on some of the

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soaring costs that suppliers are facing as they try to replace Russian gas. The money collected from consumers—households and companies—would have been used to support the

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struggling big gas importers such as Uniper, SEFE, and VNG. Habeck's gas levy plan, which never happened, was supposed to go into effect by October 1, 2022.

The Scholz coalition eventually opted to rescue the big gas importers directly by the government, making huge investments in the companies. This turned out to be a big blunder on the part of Habeck, the Green minister in charge. When Habeck tried to keep only two of three operational nuclear reactor units online, a decision eventually overruled by the Chancellor, he provoked outcries from the opposition parties who demanded keeping all nuclear reactors working until the end of 2024. Under pressure from the Greens, Scholz had to accept April 15, 2023, as the date when all the reactors in Germany will have to shut down.

### ZEITENWENDE PLEDGES IN DOUBT

In his *Zeitenwende* (historic shift) speech before the Bundestag on February 27, 2022, Chancellor Scholz responded to the Russian invasion of Ukraine three days earlier with big decisions and pledges.

Scholz announced that his government would set up a special fund for the Bundeswehr and that the 2022 federal budget would provide a one-off sum of €100 billion for that fund.

There was another important pledge: “We will now—year after year—invest more than 2 percent of our gross domestic product in our defence.”

“Chancellor Olaf Scholz was long perceived as hesitant and ambiguous. However, it was he who coined the word *Zeitenwende* in his speech in the Bundestag on February 27 and struck a completely new tone towards Russia and Putin. In his speech, which has already been described as ‘historic’, he made it clear that he is not concerned with gradual changes, not preoccupied only with spending a bit more on defence, but with a new state of affairs, and a new positioning of Germany in international politics,” according to Thomas Wimmer of Hill and Knowlton Strategies.

But as it turned out, Scholz remained hesitant and ambiguous in following up on his big promises. In the key general debate in the Bundestag on the budget on November 23, the CDU's Merz, whose party members had supported the one-off €100 billion fund to modernize the Bundeswehr, accused Scholz of *Wortbruch*—breach of promise—for not keeping his word to the parliament and the Bundeswehr for next year's military budget. Said Merz: “This government has missed the historic chance for change.” Merz noted that the defense budget that Scholz had promised would increase instead would shrink by €300 million.

Merz and his party colleagues also have been sharply attacking Scholz for not allowing heavy military equipment like tanks to be sent to Ukraine. Toward the end of September, under the headline “When will Europe learn to defend itself,” *Politico* took up the issue. In a separate article, *Politico*'s Matthew Karnitschnig noted, “Germany has, in fact, delivered heavy weapons to Ukraine, including ten howitzers, anti-aircraft systems, and other mainly defensive armaments. Critics say that the degree of military aid, which totaled €1.2 billion

as of mid-August, according to data tracked by the Kiel-based Institute of the World Economy, is not commensurate with a country of Germany's size and wealth. By comparison, the U.S. has so far committed some €25 billion in military assistance to Ukraine.”

When in the summer it became apparent that the traffic-light coalition would have to prepare Europe's largest economy and its 84 million people for the coming winter without cheap gas from Russia, it was clear that the chancellor had to be the chief crisis manager on the energy front. In this unprecedented challenge, he is supported with mixed results by economic minister Habeck from the Greens and by finance minister Christian Lindner from the fiscally conservative FDP. Lindner was able to use leftover billions from the pandemic budget and is trying to keep the constitution's “debt brake” for next year by shifting the bulk of this year's relief billions to the “off-budget” debt stock.

In fairness to Scholz, he did not hesitate to use his authority to set policy guidelines (*Richtlinienkompetenz*)

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as chancellor, as in the case of letting all three nuclear reactors operate though next spring. Also, within days of his speech, he decided to replace Germany's old Tornado jets with American F-35 jets. In preparation for his first and highly controversial “courtesy call” to Chinese President Xi Jinping in early November in Beijing, he overruled the strong objections of his coalition partners and allowed Chinese state shipping and logistics giant Cosco to take a reduced stake of 24.9 percent in a Hamburg port terminal without getting access to the terminal management.

**YOU'LL NEVER WALK ALONE**

On July 22, Scholz interrupted his summer vacation to hold a press conference in Berlin to announce new government plans to tackle the ongoing energy crisis, including a new package of relief measures for consumers and the purchase of a 30 percent initial stake in Uniper Group, Germany's largest Russian gas importer, which was threatened with bankruptcy because of the drop in deliveries from Russia and being forced to buy gas on the extremely expensive spot markets.

Scholz announced that two important legislative proposals had been agreed by the cabinet: improved housing benefits that would include more money for energy costs, and reform of long-term unemployment benefits. The latter will replace the controversial Hartz IV system by scrapping most penalties and increasing benefits. The new welfare system will be called *Bürgergeld* (citizens' allowance), and is due to go into effect in January 2023. Scholz concluded his press conference with a big promise to the German people: "You'll never walk alone."

Overcoming steep obstacles in November 2022, the *Bürgergeld* was enacted with a large majority after the CDU/CSU opposition negotiated tougher rules on asset retention and the obligations of applicants to accept reasonable job offers.

**RELIEF PLANS AND PROTECTIVE SHIELD**

Using Germany's considerable fiscal power, the Scholz coalition, faced with escalating energy costs after Russia closed its pipeline, came up with several rounds of support packages.

In early September, the Scholz coalition agreed on a relief plan worth about €65 billion to help millions of households struggling with soaring energy costs. Key measures include a pledge to cap and even redistribute huge profits made by energy companies on the back of the current crisis, increased payments to pensioners, students, parents, and the unemployed, and measures to rein in escalating electricity prices.

When the Scholz government announced that it would put into place what it called a protective shield worth €200 billion using off-balance-sheet

debt to reduce the price of electricity and gas for citizens and businesses, the German Federal Audit Court raised objections. The reaction in Brussels and in other EU member countries, especially in France, was very negative, even hostile. The huge "€200 bil-

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lion *Rettungsschirm*"—bailout—was attacked in Brussels and Paris as foul play in view of the lack of any prior consultation and ignoring the competition rules in the EU common market.

As Scholz explained, the federal government will introduce a commission to come up with special proposals for a "gas price brake" as soon as possible. Since the German government directly supported the major energy supply companies, the original proposal of a gas surcharge will not be needed.

For Habeck, the economic minister, the so-called "€200 billion protective shield" is intended to ward off "the attack by Russia, by Putin's regime on our national economy and, by destabilizing it, destabilizing the democratic order in Europe and in Germany." For Lindner, the finance minister, the "protective shield" is Germany's "reaction to the energy war for prosperity and freedom." Lindner continued, "The aim of this war was to destroy much of what people had personally built up over decades as well as the structures in small and medium-sized businesses, and the skilled trades and industry sector that have been established over the decades. The decision sent a crystal-clear response to Putin, and also conveyed a message to the people in our country: 'We are economically



*German Minister for Economic Affairs and Climate Action*  
**Robert Habeck.**

**Green Power at Work**

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strong, and we will mobilize our economic strength when necessary.”

### CHINA DECOUPLING CHALLENGES

In an op-ed for *Politico* and the German daily *Frankfurter Allgemeine Zeitung*, the German chancellor emphasized that Berlin’s goal was not to “decouple” its industry from China. “Indeed, he clearly echoed his predecessor Angela Merkel in insisting that the (unnamed but obviously identified) United States should not drag Germany into a new Cold War against Beijing,” observed the magazine’s Hans von der Burchard.

At the beginning of November, in a timely cover story, the magazine *Der Spiegel* looked at the big stakes for German companies in China. “Business as usual: German Companies Ignore Major Risks in China.” “[It] seems many haven’t learned the lesson from Russia of the perils doing business with autocratic countries.” It described a meeting with economy minister Habeck. “Business leaders responded to the minister’s wish with a shrug of the shoulders.

### Scholz tried to convince everyone that expanding Germany’s business in Asia away from China should have highest priority in the future.

‘With very few exceptions,’ said one industry representative, ‘no one wants to shut down their business in China.’ And, he says, they have already long since been looking around for opportunities elsewhere in Asia.” China was Germany’s biggest trading partner in 2021 for the sixth consecutive year, its biggest single source of imports and its second most important export destination after the United States.

Automakers Volkswagen, BMW, and Daimler and chemical

company BASF have the biggest stakes in China. To quote *Der Spiegel*, Volkswagen CEO Ralf Brandstätter “is responsible for more than thirty plants with more than 90,000 employees in China. Europe’s largest automaker sells more than one in three cars in the People’s Republic, and no other foreign market generates comparably high profits.”

Another revealing quote is from BASF CEO Martin Brudermüller, who plans to invest €10 billion in a new compound site in the southern Chinese city of Zhanjiang. While BASF does see risks in China, “What kind of risk is a company taking by giving up on half of the world market?”

The president of the European Chamber of Commerce in China, Jörg Wuttke, makes a valid point to *Deutsche Welle*: “The EU’s dependency on Russia was on two vital products, gas and oil. Whereas with China, trade relations are different and China is more dependent on the European Union. Europe also creates millions of job opportunities in China. So I don’t see a real dependency discussion there.”

Under the headline “Collateral Damage,” *Eurointelligence* notes, “As U.S.-China decoupling continues, Europe still faces old strategic dependencies on China, as well as new ones, like energy trading. The EU and its biggest member states do not yet have a coherent policy on this, but are moving a vague middle way, marked by wariness of both China and the United States.”

### NEW CHANCELLOR ON THE WORLD STAGE

When Scholz, who had met Chinese leader Xi Jinping way back as mayor of Hamburg, on November 3 embarked on his controversial one-day solo trip to Beijing—with a dozen CEOs of major German companies including BASF, Volkswagen, Siemens,

and Deutsche Bank—he had two declared objectives.

The first was to assure the Chinese leaders that China remains an important business and trading partner for Germany and Europe, and Germany

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had no wish to decouple from it. But Scholz said there should be more “reciprocity” on the Chinese side.

The second was to convince Xi to publicly confirm they “jointly oppose the use or threat of use of nuclear weapons.” As Ivo H. Daalder, former U.S. ambassador to NATO, noted: “Chancellor Olaf Scholz flew halfway across the world, with a retinue of leading German business leaders in tow, for an eleven-hour visit on Xi’s home turf. He wasn’t the first Western leader to land in Beijing since the onset of Covid-19, but he was the first to meet with the Chinese president since his total consolidation of power at the Communist Party’s Congress.”

There was a third objective that Scholz made clear on his successive trips ten days later. Scholz wants to show that Berlin sees the Asia-Pacific region as something “much greater than China.” Taking part in the Asia-Pacific Conference of German Business on November 14 in Singapore, followed by a visit to Vietnam where five hundred German companies operate, on the way to the G20 meeting in Indonesia, Scholz tried to convince everyone that expanding Germany’s business in Asia away from China should have highest priority in the future. ◆