

Policy Position

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#SickManofEurope

#GrowthModel

#EuropeanModernisation

Germany Needs a Europe Pact

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German Chancellor Olaf Scholz recently presented a new “Germany-Pact” to advance the country, following media reporting that has portrayed Germany as the “sick man of Europe” due to its waning economy. However, as Johannes Lindner and Nils Redeker observe, Europe does not play a big role in this pact. In this op-ed, originally published in *Handelsblatt*, they explain why Germany should refocus on the EU single market and develop an overall strategy for modernising the country and Europe.

Germany is once again seen as the sick man of Europe. The news that Germany will be the only major industrialized nation in the world to slip into recession this year has roiled the economic policy debate from Berlin to Munich. Since then, the country has been debating reform agendas, Growth Opportunity laws, industrial electricity prices and a new Germany Pact.

Curiously, Europe plays no role in this discussion. Newspaper commentary columns and virtual debates are filled with 10-point plans, but without mention of Europe. According to its own statement, the German government has plans for renewal of many sectors. But it is looking primarily at national solutions. Recently, the German Minister Presidents met in Brussels in a European gesture. In the end, however, the main purpose of the excursion was to ask the EU Commission President more leeway for national energy subsidies.

A new economic model - taking advantage of the European single market

This may come as little surprise. Sick men tend to feel sorry for themselves, and abdominal pain tempts navel-gazing. Besides, there is enough to do

in this country: Digitization of administration, investment backlog, education problems, shortage of skilled workers - the list of national problems is long. Nevertheless, Germany cannot rely on solving this structural crisis on its own. Individual reforms will not be enough. From energy and industrial policy to export orientation and the reduction of bureaucracy, Germany must fundamentally reorganize itself. The country needs nothing less than a new growth model. For this, Germany is more dependent than ever on Europe.

For example, Germany can only procure cheap green energy in cooperation with Europe. No national package of measures will prevent Germany from having to import a growing share of its electricity in the future. Green electricity can be produced more cheaply in the sunnier parts of Europe. In addition, Germany needs energy imports to compensate for fluctuations in the availability of renewables in the national grid. To do this, green energy needs to flow from the solar panels in Zaragoza to the steel furnaces in Salzgitter. So far, the EU lacks the physical capacity for this, the necessary digitization and the right electricity market design. According to the EU Commission, around 585 billion euros will have to be invested by 2030 to change that. In the end, there is no German transition without European transmission.

Germany also needs Europe for its industrial policy plans. In the German debate, the EU is seen above all as an obstacle to state aid. Yet a Europeanization of industrial policy would be in Germany's interest. For example, the German government has recently been celebrating that it successfully lured Intel into opening a new semiconductor factory in Magdeburg using vast sums of subsidies. However, it has gone largely unnoticed that this planned computer chip factory in Saxony-Anhalt will work closely with a new Intel plant in Wroclaw, where German semiconductors will be tested and processed into finished processors. A lot of Polish taxpayer money has gone into this. Intel is also planning further investments in France, Spain as well as Italy. The success of this German showcase project will thus depend largely on what happens in other member states. There is a more fundamental lesson here: To become the world market leader in the technologies of the future, Germany needs a division of labour and scaling across the entire EU. This then also requires more industrial policy coordination and funding at the European level.

Germany must refrain from propelling its way back to health at the expense of the EU single market, because it is dependent on it to a new degree. During the long boom of the 2010s, German exports benefited primarily from Chinese and American demand. Now Germany's most important trading partners are in open conflict with each other and investing vast sums to replace their imports with their own domestic production. In this world of new geopolitical tensions, Germany needs the EU even more urgently as a market for its exports, as a trade-policy trump-card and secure anchor. Effective „on-shoring“ of important production or of intermediate products can only be achieved via the internal market. In addition, Germany is dependent on the EU to defend itself confidently against the increasingly aggressive trade practices of China, and to be able to make attractive offers to third countries in the global race for new raw materials and trade partnerships.

Creating scope for innovation

In all of this, policy must not get bogged down in permanent subsidies or escalating isolationism. Instead, it must leave room for innovation. For this very reason, it is important that Germany knocks the dust off its own administrative structures. In many areas of the economy, however, regulation is largely determined in Brussels. An agenda of regulatory uncluttering without Europe therefore falls short. The EU's Green Deal and the digital transformation, for example, have been bundled into laws with enormous speed. And rightly so. However, in the example of regulation of financial system sustainability, in particular the taxonomy, it becomes clear that contradictions and lots of bureaucracy have

arisen in the interplay of the various regulatory requirement. These need to be critically reviewed. This is the only way to ensure that value is actually added, rather than simply wasting away piles of new paperwork. It is also only in this way that the EU can once again become the global rule-setter.

Shaping responsibility - an overall strategy for Germany and Europe

In addition to a Germany Pact, the German government needs a Europe Pact above all. The most important elements have long been under discussion. But instead of working on finding new solutions to these issues, the German government too often sits on the sidelines or steps on the brakes. It misuses the European level for national party-political competition or stands in the way of new steps, with reference to the German contribution to the still-ongoing debt-financed EU investment programme from the years of the pandemic. This does not match the urgency of the challenge - neither in Germany nor in Europe.

In its own interest, the sick man of Europe must assume more responsibility for shaping Europe. Thus, the German government should now develop an overall strategy for modernizing Germany and Europe and coordinate it closely with the EU institutions and the other member states - above all with France. This includes updated EU fiscal rules but also a new deepening agenda for the Single Market including steps towards an Energy Union and more robust instruments in trade policy. It also requires a bigger and more flexible EU budget to ensure that Europe can respond to new challenges and take over additional tasks for example on common industrial policy. And it includes starting a fundamental institutional reform process in preparation for the next enlargement. A group of Franco-German experts has just presented a number of important and workable proposals for doing so.

The political window for this is only open for a short time: the European election campaign is now getting underway, and the new Commission will be defining its work program in the second half of 2024. This is when the stakes can be hammered down and the course set. After that, there are only a few months left until the German parties have to deal primarily with the federal elections again. The political debate must take place now. There is no time national navel-gazing.

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