

## Germany faces 'hot winter'

Merkel woes and ECB easing spell weaker euro

by David Marsh

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Germany is facing a 'hot winter' as troubles pile up for Angela Merkel, the chancellor, and the European Union prepares for bruising disputes over debt restructuring, budgets and interest rates. The co-existence of several areas of divergence and rivalry – over French and German elections in 2017, Britain's potential exit from the EU, and the future of the European Central Bank's quantitative easing – makes political and economic circumstances particularly fraught.

As financial markets steel themselves for a near-inevitable rise in US interest rates on 16 December, momentum is building for a further fall in the euro. The ECB may end up realising somewhat more dramatically than expected its barely veiled desire for exchange rate depreciation – a key instrument in its bid to restore inflation rates closer to its 2% target, against the present level close to zero.

The weakening of Chancellor Merkel's hold, a result of broad opposition to her 'open door' policy on immigration, has widespread international consequences, not least for management of the euro. Even her own habitual supporters believe Merkel made a considerable miscalculation in overtly welcoming a massive tide of migrants overstressing well-heeled Germany's welfare and policing system and job-creation capacity.

There is no obvious coup against Merkel immediately in sight. Yet her most doughty (and potentially most troublesome) Christian Democrat lieutenants, Thomas de Maizière, the interior minister, and the still more heavyweight Wolfgang Schäuble, finance minister – a wheelchair-bound veteran of massive intelligence and integrity – have both been sounding mutinous rumblings in recent days.

Economics Minister Sigmar Gabriel, head of the Social Democrat party and No. 2 in Merkel's coalition government, has declared in the last few days he will run against the chancellor in the autumn 2017 election, confirming that her political partner is now officially her opponent. Merkel's predecessor, Social Democrat Gerhard Schröder, has called for migrant quotas, declaring that Merkel has 'a heart, but no plan'.

Many observers hold Merkel in high regard as a cool-headed leader who thinks first and acts later. However, her 10-year chancellorship has been marred by several hasty and ill-thought out actions. These include the announcement in early October 2008 guaranteeing all bank deposits after the Lehman Brothers bankruptcy, without any kind of law to back this up, and her quixotic decision after Japan's Fukushima nuclear disaster of 2011 to go ahead with phasing out nuclear energy in Germany, abruptly reversing an earlier plan.

With Berlin's policy credibility under fire, too, over the Volkswagen diesel emission scandal, German disarray is likely to lower the country's capacity to give a firm lead in euro area decision-making. German-inspired attempts to rein back budget deficits are coming up against heavy opposition – for a mixture of reasons – in Spain, Portugal, Italy and France, as well as in the most sensitive debtor country, Greece, which will attempt to reschedule its heavy EU debts in coming weeks.

Bundesbank President Jens Weidmann has signalled a fresh offensive against an expected ECB decision on 3 December to extend the ECB's €60bn a month bond purchases and lower the negative interest rate on ECB deposits from the present minus 0.2%. Weidmann has argued that the decline in the euro bloc's inflation rate, hovering around zero or even negative territory, is wholly due to the low oil price and does not indicate any deflationary threat.

A further area for bickering lies in the contentious field of possible concessions to the UK over Britain's attempts to renegotiate its relationship with the EU ahead of the referendum on membership in 2016 or 2017, an area that could pit France against Germany in fundamental areas of EU policy. In this strained atmosphere, the euro has only one direction to travel against the dollar – lower.

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