

## Problems beyond Merkel victory

German court complexities over QE

by David Marsh in Berlin

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Chancellor Angela Merkel appears to be heading towards easy victory in the 24 September German parliamentary elections. But considerable problems await her, particularly on the European front, should she achieve her goal of a fourth successive governing term.

Merkel, chancellor since 2005, is in a much stronger position than the leaders of France, the UK and Italy, whose combined experience in highest office adds up to less than three years, and face varying domestic challenges to their political authority. Yet, in view of unpredictable coalition talks she faces after the expected win, Merkel's position is less comfortable than it appears. The principal European difficulty focuses on the relationship with France; President François Macron has made clear he expects further significant moves towards completing the political infrastructure of economy and monetary union.

One of the most difficult issues is the relationship between the European Central Bank and European governments. The German government realises a big reason for the European recovery that has bolstered Merkel's fortunes is the ECB's powerful quantitative easing bond-buying programme, which started in 2015. But Berlin is fully aware, too, of the domestic political unpopularity of suspected QE-related unsound European money generating both potential inflation and large financial risks that Germany may end up bearing.

Related to this, German and French views on the central issue of a possible European finance ministry are far apart. Germany proclaims its willingness to give up sovereignty over European decision-making but wishes a future euro area finance ministry to have only minor additional budgetary powers. France wants to transfer only limited sovereignty but gain an appreciable European budget – an option that Germany, as the European Union's largest creditor and financial contributor, rules out.

Merkel's conservative grouping of the Christian Democratic Union and Christian Social Union is far ahead in opinion polls, with an indicated 38% of the votes against 23% for the challenger Social Democratic Party (SPD). The big question is which party comes third. Alternative for Germany (AfD), the anti-euro, anti-immigrant far-right group, is near-certain to exceed the 5% of votes needed to enter parliament after 24 September, marking the first time since the early post-war years that a party to the right of the CDU/CSU has entered the Bundestag. Currently polling around 9%-10%, AfD may achieve third place, buoyed by unease over immigration and the ECB's QE.

Martin Schulz, leader of the SPD – junior partner in the current Berlin coalition with the CDU/CSU – did little to improve his chances in a bloodless TV debate with Merkel on Sunday evening where he gave an earnest but lightweight performance. Merkel successfully kept up her customary veneer of reasonable middle-of-the-road views and polite competence. Schulz wishes to keep alive the possibility of a further 'grand coalition'. Merkel, on the other hand, would like to reforge a coalition with the CDU/CSU's traditional partner, the liberal Free Democratic Party, which failed to cross the 5% parliamentary hurdle in the previous election four years ago, but looks likely to gain a place after 24 September.

Reflecting the effect of the AfD's parliamentary debut, the CDU/CSU and FDP by themselves will not have enough seats for a parliamentary majority. If she wishes to avoid another alliance with the SPD, Merkel will have to negotiate on sharing power with the Green ecology party as a hitherto untried coalition partner for the CDU/CSU.

Merkel's policies on Europe and France will be constrained by probable coalition with the FDP, which will take a harder line on help for weaker nations as well as on any complexities resulting from QE. The anticipated presence of the AfD will make parliamentary debates on Europe more robust than in the past.

Furthermore, when German ministers and deputies return from their holidays and their election tours this month, as a result of down-to-earth discussions with voters they are normally more nationally minded and less 'European' than beforehand. This will be reflected in parliamentary discussions after the election.

Political complexities could arise from the German constitutional court's announcement in mid-August that it finds 'important reasons' for believing that ECB's QE contravenes the European ban on monetary financing of budget deficits and oversteps the limits of the central bank's mandate.

The constitutional court has asked the European Court of Justice to answer key questions before the German court gives a verdict next year. The action will not have any immediate impact on the ECB's plans for an 'orderly exit' from the QE programme, but could increase political pressure after the election for the programme to end earlier.

In a widely overlooked part of the announcement, the court pointed out Germany could be liable for additional large financial risks stemming from possible losses by other national central banks' purchasing their own country's government bonds. The German government and the Bundesbank believed this had been ruled out when the QE programme was decided in January 2015. Clarification of this issue will be one of the most important parts of a future constitutional court judgement – and could, in the worst outcome, lead to legal action between the German government and the ECB.

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