rethink the recovery

IS GERMANY TAKING A ROCKET TO A TRANSFORMED FUTURE OR CATCHING AN OLD TRAIN BACK TO 'NORMAL'?

German recovery plan analysis:
„Das Konjunkturprogramm für alle in Deutschland"

Of the €130 billion German Recovery Budget:

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Finance Watch
Making finance serve society

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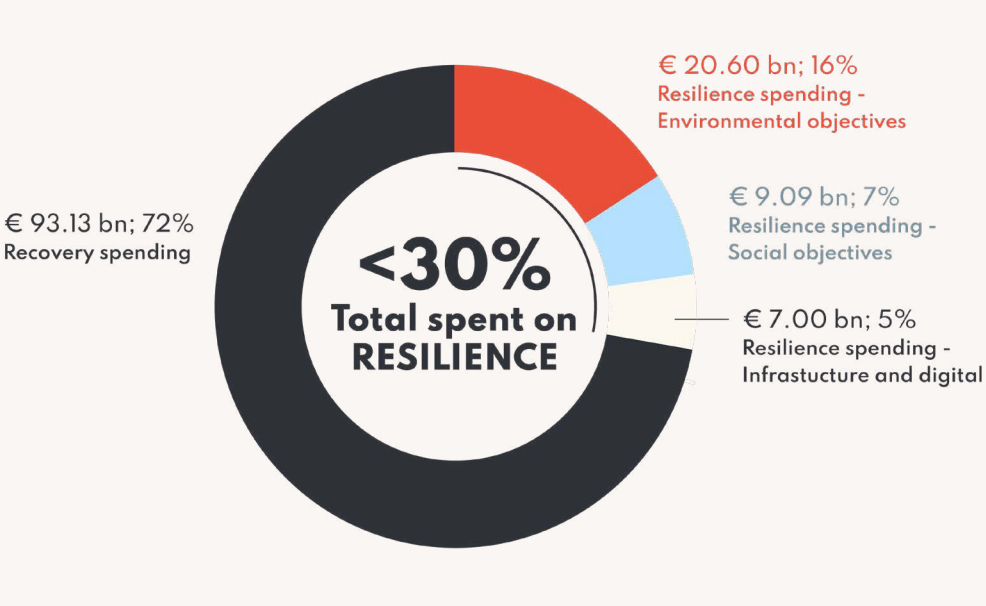
EXECUTIVE SUMMARY

Finance Watch has analysed the German fiscal plan **"Das Konjunkturprogramm für alle in Deutschland"** put in place by the German government. The plan aims to help repair the immediate economic and social damage brought about by the coronavirus pandemic as well as make the economy more sustainable and resilient to future shocks. **Presented officially in June 2020**, the plan will be partially financed by the funds provided by the Next Generation EU Recovery and Resilience Facility (RRF) in accordance with the criteria defined by the RRF Regulation text.

Finance Watch assessed the proposed German policy measures on their environmental and social sustainability as well as contribution to economic recovery vs resilience objectives. For this, the time horizon over which the measures are expected to have their effect (long-term vs short-term), and the alignment with the strategic objectives were taken into account. Such objectives include, among others, the reduction of greenhouse gas emissions, energy transition, digital transformation, social sustainability.[1] **Resilience measures** were defined as long-term oriented and expected to have transformative economic effects rather than restore the pre-crisis economic situation, which is the main objective of recovery-oriented measures.

Based on the analysis, the **breakdown of the total fiscal plan spending of €130 billion** is as follows:



1 Expert judgement was used to execute the assessment. No account of the starting conditions in the country was taken, which might accelerate or slow down the transition towards sustainability and resilience.

Summarizing the results of the Finance Watch review:

- Resilience-oriented measures account for less than 30% of the planned budget.
- Seventy percent of measures aim to restore the demand-side of the economy in the short-term. Among these, VAT reductions, Kurzarbeit money and short-term emergency support for SMEs account for more than 50% of the planned budget.
- Environmental sustainability-oriented measures contributing to the resilience objective account for only around 15% of the overall budget. Also, the strength of the sustainability component of these measures requires enhancement.
- Missing linkage between planned measures and Germany´s long-term energy and climate objectives.
- Case evidence suggests that the funds have already been used to the benefit of powerful industry players rather than transform the overall economic structure and ensure its resilience to future shocks. Noteworthy examples include:
    - Lufthansa bailout with no specific business oversight conditions from the government
    - Loan for the multinational conglomerate Thyssen-Krupp
    - Luxury cruise shipbuilder MV Werften bailout without receiving guarantees that job cuts will be avoided (also refer to the comments by Euractiv)
    - See this Coronaid-Tracker for an overview of companies that received state support, and their presence in tax havens.

The measures put in place as per the plan should be viewed in the broader **context of** the EU economic governance and fiscal framework. The framework comprises a complex architecture of rules constraining Member States' fiscal policy, combined with a system of governance and tools aimed at enforcing these rules. The most significant of these rules are the 60% limit on the government debt-to-GDP ratio and the 3% limit on the budget deficit-to-GDP ratio, including the corresponding adjustment mechanisms in case of limit deviations. These limits do not properly account for the economic cycle, quality of spending and impacts that environmental and social imbalances have on long-term debt sustainability. Thus, the existing **fiscal framework reinforces policy short-termism and prevents the EU countries from reaching their social and environmental goals.** Even though the rules were temporarily suspended due to the pandemic situation, potential return to fiscal austerity could **break the recovery.** Concerns regarding breaking the existing fiscal rules are highly vocal across the German political landscape and society, as highlighted in the ZDF summary.

Conclusions reached by Finance Watch are consistent with…

➜ **the following expert assessments and databases:**

- Institute for Sustainable Development and International Relations (IDDRI) analysis
- Greenness of Stimulus Index produced as part of the Finance for Biodiversity Initiative (F4B) to assess if the global pandemic stimulus measures will help boost global resilience to climate and biodiversity risks
- Green Recovery Tracker by Wuppertal Institute and E3G – Third Generation Environmentalism (summary)
- IMF database summarising key fiscal measures governments have announced or taken in selected economies in response to the Covid-19 pandemic

➜ **and opinions:**

- German Institute for Economic Research (Deutsches Institut für Wirtschaftsforschung)
- News portal watson referring to academic sources

COUNTRY PLAN'S CONTEXT

The German recovery plan was announced on the 3-4th of June 2020 by the German coalition made up of CDU/CSU and SPD political groups. The plan encompasses 57 measures with three sets of priorities: boost demand, promote investments and prepare for the future. One main plan feature is that its implementation will be conducted prior to and after German federal elections taking place on the 26th of September 2021. Thus, a set of policies and regulations attached to the plan will need to be executed in a context where the political debate may be changing.

MAIN TAKEAWAYS

The details of the German plan do not provide evidence that resilience forms part of the current plan's ambition. The German plan largely comprises recovery measures and is therefore characterized by its emergency nature. Out of a total budget of €130 billion, emergency and recovery measures account for €93 billion. Only €37 billion worth of measures are being assessed as contributing to develop resilience with spending on healthcare, transportation infrastructure, green mobility and digitalisation (with a 5G broadband network).

Strong public support is designed to mitigate the effects on the economy from decreased consumption through two flagship measures: Temporary unemployment benefits ("Kurzarbeit") and lower value-added tax rates. Both recovery-led measures are deemed to support the

final demand for products and services stemming from low-income earners. Those measures were planned for a temporary period ending on the 31st of December 2020 with extensions provided into 2021, notably for the taxpayers heavily affected by the crisis. While these emergency demand-led measures are more sizable and impactful in the context of an activity downturn, those measures may need to be reset later during the economic recovery phase.

Sustainability proofing of the plan needs further improvement (see Graph 1). Among environmental objectives, targets on green mobility, streamlining of environmental subsidies and taxation echo the EU Green Deal and the 2050 climate neutrality goals. The review did not find, however, any clear sustainability assessment attached to the investment plans on transportation, mobility and renewables energies. The social sustainability dimension of the long-term measures is satisfactory. Unlocking sustainable jobs in the post-Covid-19 timeframe may be a way to tackle inequalities.

RESILIENCE ASSESSMENT

The country assessment found that a vast majority of the measures are of the recovery nature. Resilience gaps are being highlighted below, in correspondence to the definition that Finance Watch provided in the report "10 Principles for a Sustainable Recovery", presented on the 2nd of October 2020 (see Annex 1 for details).

- Long-term orientation of the measures to support their resilience is not presented in the plan.

- From both climate and resilience perspectives, the plan fails to outline details on its ability to contribute to the national energy and climate objectives. The measures show disconnect with environmental benefits in different domains such as climate mitigation, adaptation, resources' use, air pollution or biodiversity protection.

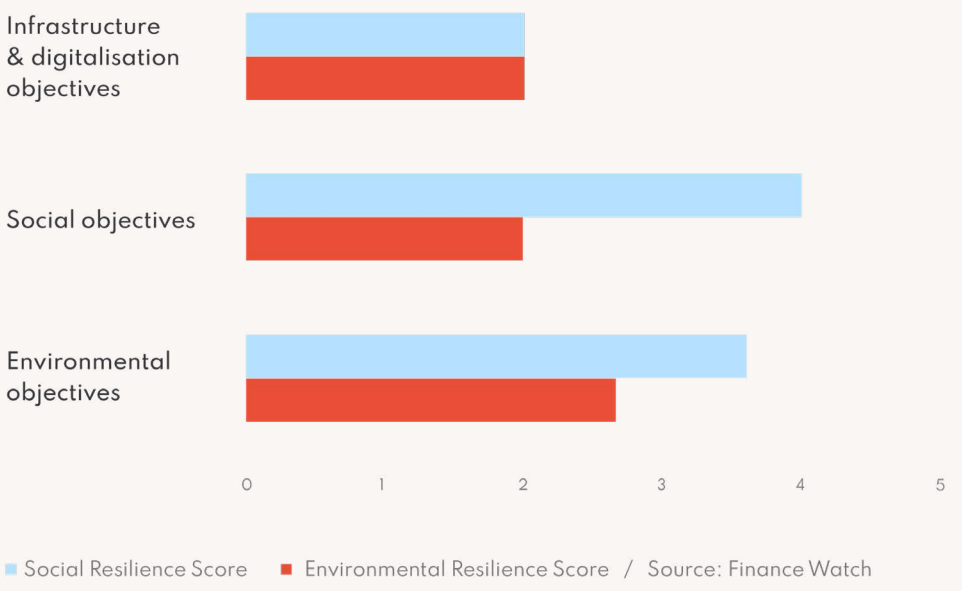
The assessment of the resilience dimension of the measures presented in the German plan represents a first step towards an integrated fiscal policy. Indeed, the next 10 years will be crucial when it comes to achieving social cohesion. And, as recommended by Finance Watch, fiscal sustainability requires a more proactive public debt management under an integrated climate and fiscal stance at EU level.[2]

Sustainability assessment of resilience measures

To better understand the sustainability component of the measures, the scores below shed light on the measures considered as both long-term oriented and resilient. Annex [2] provides more details on the budgeted funds for the respective group of objectives – environmental, social, infrastructure & digital. By definition, this score does not include the measures exclusively oriented towards recovery.

2 https://www.finance-watch.org/publication/10-principles-for-a-sustainable-recovery/

Graph 1: Sustainability scores of German fiscal measures / 1-5



COUNTRY DETAILED ASSESSMENT

Social and cohesion measures. 65% of the plan addresses cohesion and solidarity-related challenges via measures dedicated to social objectives based on the Finance Watch grouping. The three main social measures account for the budgeted amount of €51 billion: i) Employee short-term benefits (Kurzarbeit), ii) Value-added tax reductions, iii) Family and single parent allowances, guarantees on social contributions, basic income for job seekers, support for apprentices, assistance to the cultural sector, KfW loans to NGOs. Short-term benefits (Kurzarbeit) have been extended until the end of 2021.[3] In the cohesion pillar, only education and health spending have been selected as resilient. They represent €9 billion of spending. All other measures, including liquidity and protection provided to small corporations, individuals and employees, aim to improve the purchasing power of consumers and have been classified as recovery-led measures.

Environmental measures. Green mobility stands as a priority of the fiscal plan with an objective of 7-10 million electric vehicles (EVs) on the German roads in 2030. Significant financial incentives are being provided for purchases of EVs and to low-emissions heavy goods vehicles. Sales of electric vehicles – defined as plugin hybrid and battery vehicles – during the pandemic show some high levels of resilience throughout the European Union (see the case illustration below). ▼

3 https://www.bundesfinanzministerium.de/Content/DE/Standardartikel/Themen/Schlaglichter/Konjunkturpaket/2020-06-03-eckpunktepapier.pdf?__blob=publicationFile&v=9

Case illustration: **Electric mobility**. Incentives provided to consumers to move to electric mobility can be illustrated by the number of new vehicle registrations reflecting the market progression of EVs. EVs sales fell 2.5 times less in April 2020 as compared with the decline in the total number of passenger car registrations.[4 5] EV sales figures contribute to putting the country on track to achieve its environmental objectives and therefore long-term resilience.

The German automotive industry announced before the pandemic a series of moves towards **electric mobility** and the fiscal plan further demonstrates the ambition of Germany to become a leader in the field. **This evolution should contribute to building environmental resilience, as new mobility patterns aligned with a lower carbon footprint will lead to lower greenhouse gas emissions**. The move to green mobility provides an illustration of the resilience that can result from the vehicle fleet replacement programme, when complemented with the purchase support measures (Temporary Federal Ecobonus) in the electric mobility sector.

Still, certain measures of the plan may sound like "old wine in new bottles", especially when it comes to green mobility or to the hydrogen plan, as they refer to pre-existing national strategies. Meanwhile, the fact that investment measures are being recognized in this stimulus plan can also be read as a sign of political will given that the plan has been agreed by the CDU-CSU political coalition ahead of the next elections set for September 2021.

Case illustration: The **National Hydrogen Strategy is central to the plan's resilience** assessment given that it represents €7 billion of additional measures. Hydrogen infrastructures form part of the Energiewende and the EU Green Deal (with the Clean Hydrogen Alliance) so that the hydrogen strategy would also benefit from multiple financing sources. The national strategy being integrated into the recovery plan enhances its execution capacities.

Case illustration: A €5 billion equity injection in **Deutsche Bahn** has been **excluded** from the scope of the scoring. The equity financing instrument lacks environmental or social conditionality.

The definition of **infrastructure measures** focuses more on **digitalization**. Investments in artificial intelligence are being expanded €2 billion. A €5 billion investment is being made in a public entity charged with 5G deployment by 2025.

4 International Energy Agency 2020 - Global EV Outlook 2020 https://www.iea.org/reports/global-ev-outlook-2020

5 https://cordis.europa.eu/article/id/422220-covid-19-the-resilience-of-the-electric-car-market

CONCLUSIONS AND WAY FORWARD

- **Plan resilience component.** The German stimulus plan offers new opportunities for investments along possibly new economic models in sectors such as low carbon mobility, health, digitalization as well as education. The success and resilience of the plan will require, however, more connections with defined environmental and social dimensions and/or indicators, since wider social reforms may also be implied by the announced measures. The €20 billion Value Added Tax exemptions initially had been described as a plan centerpiece, but these might not be sufficient if the economic recovery was to remain more muted in 2021 and beyond.

- **Sustainability of plan hinges upon its execution** through laws and bills that will need to go through the Bundestag in the context of an election campaign. In this context, some voters may start questioning both the planned composition of measures and underlying assumptions within the plan.

- **Environmental sustainability: alignment with coal and fossil fuel phase out.** According to the European Commission assessment of Germany's National Energy Climate Plan, the country is on track to achieving its 2030 goal to reduce greenhouse gases emissions by 40%.[6] The Commission assessment highlights that Germany has indicated a timeline to phase out coal subsidies together with expiry dates for other fossil fuel subsidies. The plan's resilience could be improved by establishing links between the phase out commitments as well as measures and reforms embedded in the plan.

- **Environmental sustainability: New environmental fiscal measures** are introduced in the plan. In particular, the plan indicates that carbon emissions will play a greater role in determining motor vehicle tax rates, as clean cars will be subject to lower rates than high-emission cars from 2021 onwards.

- **Planning long-term ecological and social resilience proves key** to consolidating the centre of gravity of the plan, enhancing its impact and facilitating its adoption by citizens, their representative bodies and/or by non-governmental organizations. The Institute for European Environmental Policy defines five future-proof sustainability tests for any recovery or stimulus plans[7].

- **EU economic coordination and governance** will be on the political agenda in 2021 and debate will take place on the EU spending rules and conditionality (EU fiscal rules).[8] In this context, the national recovery and resilience plans (NRRPs) submitted by the Member States to the European Commission represent an opportunity to embed ex-ante long-term sustainability criteria. The German national stimulus plan represents an opportunity to provide a reference pathway in the process, alongside with the plans of the other Member States of the European Union.

6 SWD(2020) 904 final, https://data.consilium.europa.eu/doc/document/ST-11897-2020-INIT/en/pdf.

7 https://ieep.eu/news/europe-s-recovery-plans-must-pass-five-sustainability-tests

8 Conditionality or macro conditionality are the rules linking EU spending to the Rule of Law or other challenges identified in a national macro assessment.

ANNEX 1: FINANCE WATCH ASSESSMENT PRINCIPLES

The Finance Watch review includes an assessment of the individual measures within fiscal plans announced in 2020 by France, Germany and Spain. Finance Watch assessed the proposed policy measures on the subject of their contribution to environmental and social sustainability, as well as contribution to economic recovery versus resilience objectives. For this, Finance Watch took into account the time horizon – long-term versus short-term – over which the measures are expected to have their effect and the alignment with the strategic objectives. Such objectives include, among others, the reduction of greenhouse gas emissions, energy transition, digital transformation and social sustainability.

In analysing each of the fiscal measures, Finance Watch differentiated between two sets of measures:

- measures that improve **resilience** of the economy and society,
- measures that are of short-term or emergency nature and therefore considered as **recovery-driven.** These measures are mostly targeted at restoring the pre-crisis economic situation.

Each individual investment or reform measure has been characterized as being either resilient or driven by recovery considerations. Resilience measures were defined to be long-term oriented and expected to have transformative economic effects beyond 2021 up until 2030-2050. As a result, resilience-based measures relate to investments, which enhance the ability of economies and societies to withstand future shocks and thus be more prepared to minimize environmental risks and maximize social justice. This assessment can be seen as a decomposition of each fiscal plan into two sub-parts: the resilience part and the recovery part, as illustrated in Annex 2.

For more information, the methodological note can serve as a reference.

ANNEX 2: FINANCE WATCH MATRIX - GERMANY

Breakdown of National Recovery Resilience Plans

Source: Finance Watch

Amounts (Million Euros)	Environmental sustainability objectives (Pillar 1)	Social sustainability objectives (Pillar2)	Infrastructure & digitalisation objectives (Pillar 3)	Not scored	Plan based Resilience - Recovery Mix (%)
German Stimulus Package	34,100	83,715	7,000	5,000	-
Resilience	20,600	9,090	7,000	-	28%
Recovery	13,500	74,625	0	5,000	72%

ANNEX 3: GERMAN COUNTRY FORECAST – ANNUAL GROWTH SURVEY

	2020	2021	2022
GDP % change	-5.6	3.5	2.6
Unemployment rate (%)	4.0	4.0	3.8
General government balance[9] as % of GDP	-6.0	-4.0	-2.5
General government debt as % of GDP	71.2	70.1	69.0

Source: European Commission - Country forecasts - Annual Growth Survey - 2020[10]

Gross domestic product (GDP) is forecast to fall by 5.6% in 2020 compared to 2019 and investments are expected to be back to their 2019 level as early as 2021, while also depending on the recovery of industrial output. The unemployment rate will settle at 4.0% in 2020 and 2021 and 3.8% in 2022. These economic forecasts as published in the Annual Growth Survey 2020 do not include Recovery Resilience Facility economic growth multiplying factor. According to European Commission economic forecasts, German public debt-to-GDP ratio will slightly exceed 70% in 2020 and 2021 due to the automatic stabilizers and fiscal measures.

Link to the Stimulus Plan

Link to the German National Energy and Climate Plan

9 General government balance includes the balance of the central government, state/regional governments (applicable in Belgium, Germany, Spain, Austria and Switzerland), local governments and social security funds.

10 https://ec.europa.eu/info/business-economy-euro/economic-performance-and-forecasts/economic-performance-country/germany/economic-forecast-germany_en

About Finance Watch

Finance Watch is an independently funded public interest association dedicated to making finance work for the good of society. Its mission is to strengthen the voice of society in the reform of financial regulation by conducting advocacy and presenting public interest arguments to lawmakers and the public. Finance Watch's members include consumer groups, housing associations, trade unions, NGOs, financial experts, academics and other civil society groups that collectively represent a large number of European citizens. Finance Watch's founding principles state that finance is essential for society in bringing capital to productive use in a transparent and sustainable manner, but that the legitimate pursuit of private interests by the financial industry should not be conducted to the detriment of society. For further information, see www.finance-watch.org

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