

## It's the economy that counts!



Dr. Michael Heise on Global Economics  
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**The new coalition government has set out with the goal of modernizing Germany and daring to make more progress. Dr. Michael Heise explains why the right economic policy plays a very important role in achieving these ambitious goals.**

**Our country is to become greener, more digital and faster, while advancing freedom, democracy and justice. With the new mission statement, the coalition government wants to trigger a departure into a modern and progressive future. The coalition agreement underpins this objective with a very comprehensive list of political declarations of intent and concrete agreements between the parties for the next four years.**

However, one can expect that the political program of the first three-party coalition in Germany will still be discussed intensively - for example, with regard to which steps have priority and with which concrete measures the partly still generally formulated political goals will be tackled. Some measures will remain controversial and some will prove unfeasible due to a lack of funds.

### **The ability to finance will be a difficult hurdle for many**

Since the constitution's debt brake is not to be fundamentally changed, new borrowing will have to be much lower again from 2023 onwards after the pandemic exception years. The coalition agreement does not quantify how much money will be needed. What is clear, however, is that it will be a lot. In the original wording, for example, "the 2020s are to be a decade of investment in the future, particularly in climate protection, digitization, education and research, and infrastructure.



To this end, it says, a policy is being pursued "that will significantly increase investment - both private and public." In addition, there will be a need for funding due to rising social spending, as already announced by the Ministry of Family Affairs, for example, and as planned in the areas of the Ministry of Labor and the Ministry of Health.

What can be done and how successful the government will be will depend crucially on the course of economic development. One is inclined to recall Bill Clinton's statement "It's the economy, stupid". Only if the German economy returns to a growth course after overcoming the pandemic can the government expect to receive the urgently needed tax revenues it needs for its ambitious projects. And only if incomes develop positively will the additional burdens for climate protection, the energy turnaround or the welfare state be accepted by citizens and voters.

## The coalition agreement lacks a holistic view of economic policy

Benötigt What is needed, therefore, are favorable framework conditions for an increase in employment, for declining unemployment and the greatest possible scope for productivity-oriented wage increases. In addition, it should be beyond dispute that the green and digital transformation of the economy must be driven primarily by private-sector investment in the renewal of the capital stock and by technological innovation. This also requires a strong and competitive economy.

The goal of strengthening the economy in order to master the major challenges is mentioned several times in the coalition agreement, but is not backed up by a comprehensive plan of action. It would have deserved its own chapter and a holistic approach. Individual starting points are scattered throughout the government plan. It is certainly true that government investments in infrastructure and spending on research and education help strengthen the economy. They provide short-term economic stimulus and help improve productivity in the long term. However, when assessing the competitiveness of the economy and the attractiveness of Germany as a business location, we need to look at more than just the infrastructure, which can be described as dilapidated in some areas.

The important framework conditions for the economy also include things like wage costs, ancillary wage costs, energy costs, tax burdens, the availability of qualified workers, rapid planning and approval processes, legal certainty, bureaucratic costs and more.

In the sum of these factors, Germany is by no means starting the economic transformation from pole position. Some things are very good in this broad catalog of framework conditions in Germany, but in the overall picture, the location clearly falls behind others. Capacity and investment growth has been relatively weak for years, resulting in low productivity gains. The role of start-ups and the dynamics of economic innovations in Germany could also be improved.

The competitiveness of companies and jobs is also very dependent on energy and environmental policy. We have made only moderate progress toward the goal of CO2 neutrality, but this has been associated with high costs in many areas, not least with above-average electricity prices for companies and consumers. Renewable energies are being expanded, but remain partly unused because energy networks and storage media are lacking. As a result, jobs are endangered rather than created, since companies are given incentives to relocate production abroad with more favorable cost conditions.

## What the new government should do in terms of economic policy

The new government is expected to pursue an economic policy that addresses these weaknesses. One starting point would be Germany's very high tax and contribution ratio by international standards. Unfortunately, explicit reforms are not on the agenda. The only things currently under discussion are tax-free payments into the pension fund and a "super write-off" for investments in climate protection or digitization projects, which still needs to be defined in more detail. As far as the tax rate is concerned, additional burdens are foreseeable simply due to demographic developments in the coming years.

It would therefore be all the more important for the coalition to make good on its announcement to relieve the economy of bureaucracy, to achieve faster (digital) planning and approval processes and to lead the state into a digital future. All of these would be significant advances, especially since reducing bureaucracy does not incur any direct costs. However, bureaucracy reduction and leaner procedures have been repeatedly promised by previous governments, but never actually implemented. Experience shows that the argument of bureaucratic burdens is quickly brushed aside when "higher" political goals are to be achieved, as is the case with regulations on the minimum wage, environmental protection, the Supply Chain Act or financial market regulation. If the government were to make progress in reducing bureaucracy and speeding up procedures, that would be a real seal of approval.

## Conclusion: Policymakers need a holistic approach

Germany needs a strong economic base to manage the green and digital transformation and to keep the social systems financially viable in the coming times with a smaller workforce and more people entitled to benefits. Demographic change in particular will pose considerable challenges for the social systems and the public budget, which are not given top priority in the coalition agreement. It is up to policymakers to create the conditions for a strong economic base by setting the right framework conditions that not only secure the competitiveness of the economy and the attractiveness of the location, but also improve it as much as possible. Insofar as additional burdens are placed on companies and employees, for example in order to achieve environmental or social policy goals, relief should be considered elsewhere. On the other hand, Germany would lose prosperity and economic strength if numerous additional burdens were imposed on business and employees because all areas of politics, from social policy to environmental policy to health policy, seem to have good reasons for higher charges, taxes or stricter regulations and bans. Taking a holistic view of the framework conditions is the core task of economic policy and will be crucial to the success of the new coalition government. Whether the new government will take such a view remains to be seen.

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