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Economic Briefing

What the German election results mean for economic policy

24 February 2025

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A future coalition of CDU/CSU and SPD is likely to agree on more money for infrastructure and ultimately push this through despite a blocking minority of the right-wing AfD and the Left Party. That would be good for business. However, the CDU/CSU and SPD have significantly different opinions in many areas of economic policy, such as tax, social and climate policy. This lowers the likelihood of a fresh start in economic policy, which is urgently needed after five years of stagnation in Germany's GDP.

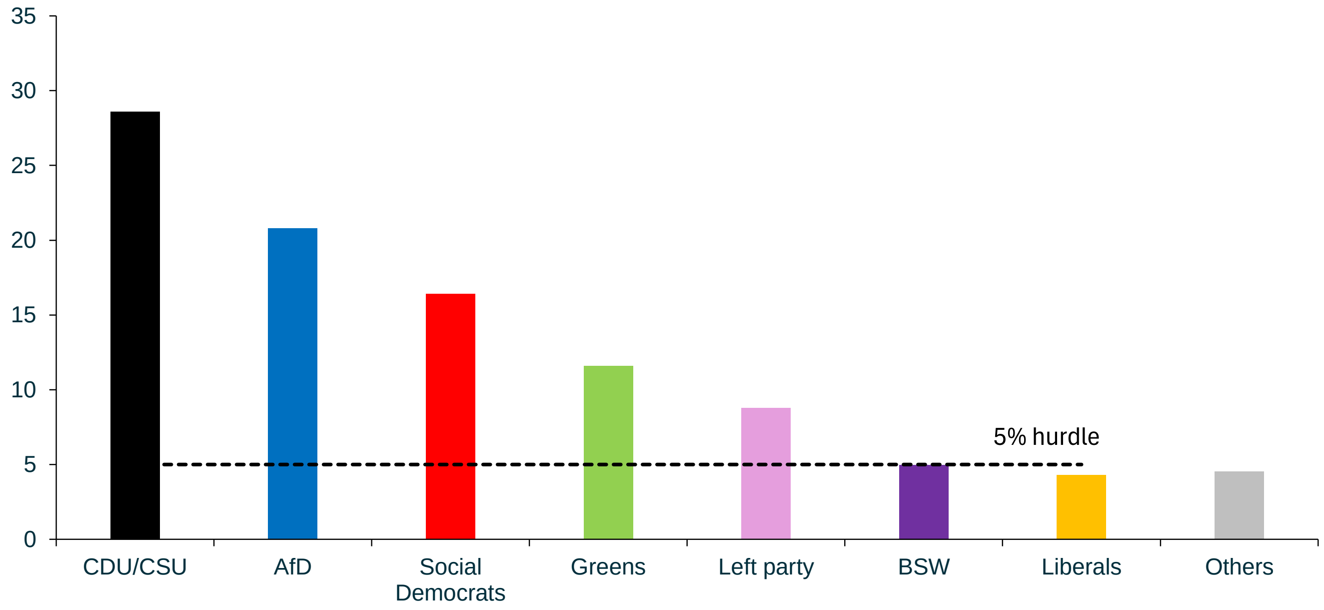
The Christian Democrats (CDU) and their Bavarian sister party CSU clearly won yesterday's general election, even though their share of votes fell short of expectations at 28.6% (2021: 24.1%). The members of the former ruling coalition had a disastrous election night. While the Greens' losses of a good three percentage points (11.6% after 14.8%) were still limited, the Social Democrats (SPD) (16.4% after 25.7%) literally plummeted, the worst result in post-World War II Germany. With 4.3%, the Liberals (FDP) will no longer be represented in the Bundestag.

The parties on the left and right of the political spectrum were clearly strengthened. The right-wing AfD doubled its share of the vote to 20.8% (2021: 10.3%) and the Left Party also increased significantly from 4.9% to 8.8%. The new left-wing party Bündnis Sahra Wagenknecht (BSW), a split-off from the Left Party, fell just short of the 5% threshold with 4.972%.

Now that the FDP and BSW have failed to reach the five per cent threshold according to the provisional final result (Chart 1), the election winner, the CDU/CSU under Friedrich Merz, will probably form a government with the SPD. These parties together have a narrow majority of 328 votes in the new Bundestag (630 seats in total, Chart 2). However, the AfD (which has doubled its share of the vote) and the Left Party have more than a third of the seats in the Bundestag and therefore a blocking minority in the event of a possible amendment to the Basic Law, the German Constitution.

Chart 1 - CDU/CSU win the election, BSW and Liberals out

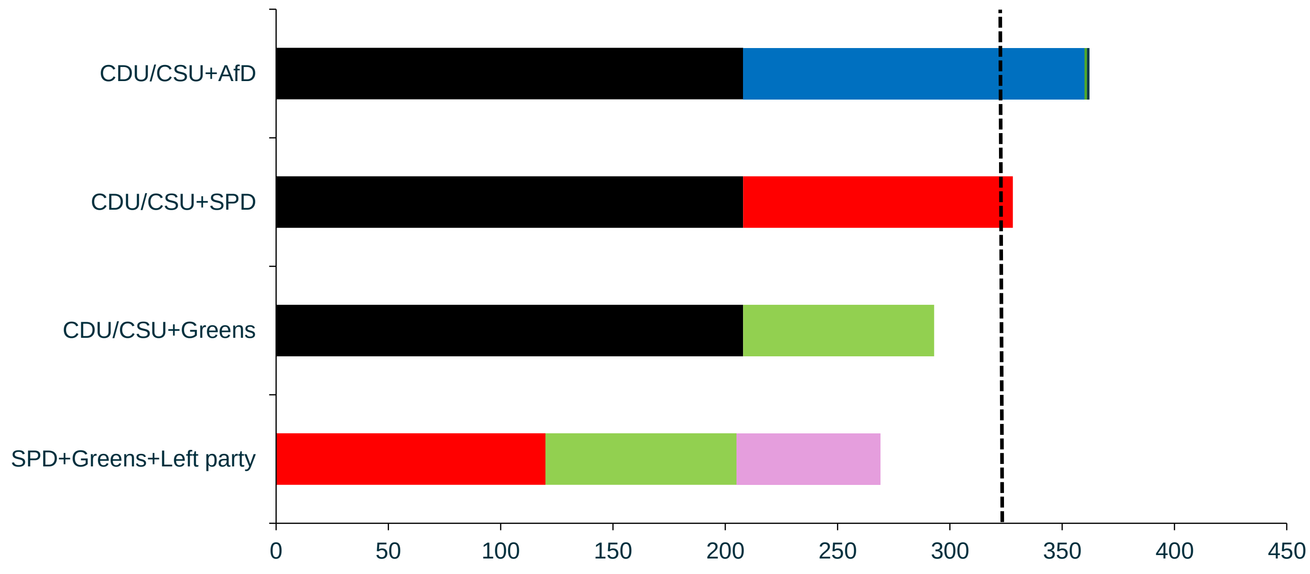
Share of votes at yesterday's general election, in percent



Source: Bundeswahlleiter, Commerzbank Research

Chart 2 - CDU/CSU and SPD can form a new government

Number of seats of different party combinations in the future Bundestag; dashed line: absolute majority of 316 seats



Source: Bundeswahlleiter, Commerzbank Research

Where will the money for the Bundeswehr and infrastructure come from?

A major challenge for a new federal government will be to mobilize more money for the armed forces and infrastructure. In order to increase defense spending from the current 2% to 4% of GDP, for example, the federal government would have to cut non-defense spending by a quarter if this is not to be financed by additional debt. This would hardly be politically feasible, even if there is considerable scope for savings with regard to social spending or the often inefficient climate policy. But setting up a new shadow budget ('special fund') for the Bundeswehr would require a two-thirds majority, which the CDU/CSU and SPD do not have, even with the support of the Greens. At best, the Left Party's approval would be conceivable if the government were to combine a special fund for the Bundeswehr with a special fund for higher infrastructure spending or generally relax the Constitutional debt brake, for example by excluding infrastructure investments from the debt rule. If this does not succeed, the only remaining option from a political perspective would probably be to suspend the debt brake with reference to an ‘extraordinary emergency situation’ that is beyond the ‘control of the state’ and would ‘significantly impair the state's financial situation’ (Article 109, paragraph 3 of the Basic Law, the Constitution). This would be possible with a simple majority, although the CDU/CSU has always been opposed to suspending the debt brake and it is also not certain that this would stand up to scrutiny by the Federal Constitutional Court.

A fresh start in economic policy?

When it comes to other economic policy areas, the CDU/CSU and SPD often have different views on how to make Germany an attractive location for companies again.

While the CDU/CSU wants to reduce taxes for all companies, the SPD wants to ease the burden on companies through an investment premium and even increase the tax burden on higher incomes, which would also affect many entrepreneurs. In terms of social policy, the CDU/CSU wants to reduce social spending, while the SPD is reluctant to make deep cuts. When it comes to the important issue of reducing bureaucracy, the parties also have different views on which regulations are unnecessary.

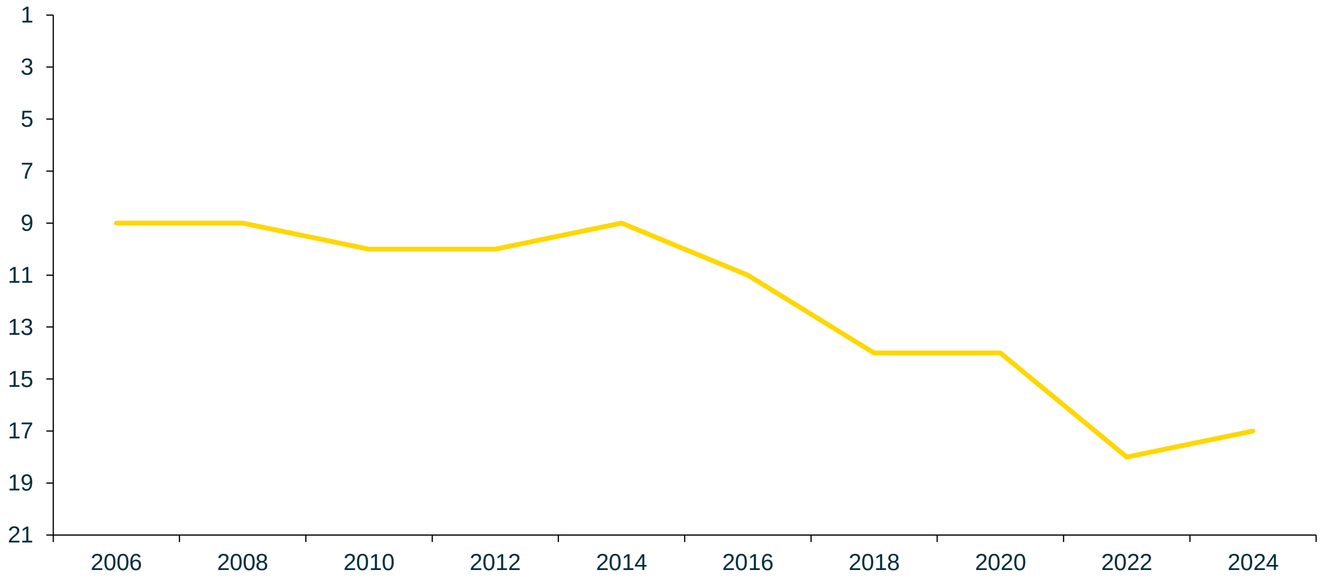
In the end, an upcoming coalition is most likely to agree on more money for infrastructure. That would undoubtedly be good for companies suffering from poor infrastructure. But all in all, the differences in the economic policy positions of the potential coalition partners largely outweigh the similarities. This dampens the hope that there will be a fresh start in economic policy. We still only expect marginal growth of 0.2% for 2025.

Eroded competitiveness

The stagnation of the German economy over the past five years, which is largely due to a deterioration of competitiveness of the German economy since the Merkel years, shows how great economic policy challenges for the new federal government are. While Germany still ranked in the middle of the 21 countries analyzed in the Family Business Foundation's country index in 2014, it is now in 17th place (chart 3). According to this study, the main weak points are the comparatively high taxes and labor costs as well as bureaucracy.

Chart 3 - Germany on a downward trend ...

Germany's ranking in the “Family Business Country Index” and its subcomponents among 21 countries



Source: Stiftung Familienunternehmen, Commerzbank Research

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This report was completed 24/2/2025 08:07 CET and disseminated 24/2/2025 08:07 CET.

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