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GERMAN "WUMMS" vs. FRENCH "RELANCE": WHO DOES IT BETTER?

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To boost growth after the Covid-19 fallout, Germany and France have introduced large stimulus packages, which, in terms of magnitude, are playing in the same league (4.3% of 2019 GDP in France vs. 3.8% in Germany). Digging below the surface, however, unveils deeply diverging approaches to boost the recovery. In particular, the two economies appear to have taken cues from each other's economic rule books, with France focusing above all on supply side support (see Appendix for details) while German fiscal policy has taken a textbook Keynesian spin.

Betting the house on the consumer in Germany.

- In Germany, the consumer is at the heart of fiscal stimulus efforts: Around 25% of Germany's fiscal "Wumms" - i.e. the EUR130bn stimulus package put forward in early June - directly benefits households. The vast majority of these measures are frontloaded in the hope that this will boost consumer confidence and in turn unlock excess household savings at a crucial stage of the economy's recovery. The bet centers in particular on a temporary VAT tax cut worth EUR20bn in the second half of 2020. But Germany's newfound consumer love does not end there. While not included in the *Konjunkturpaket*, additional measures aimed at propping up employment and income, namely easier access to *Kurzarbeit*, the top-up to income replacement rates as well as the recent extension of the scheme's duration, all of which together will cost a cool EUR35bn, should not be ommited in this calculation.
- Meanwhile, in France the consumer is getting very little direct support: In its stimulus plan, the French government allocates EUR800 million for direct transfers to students and those with low incomes.The French authorities rule out potential VAT cuts with the rationale that the current VAT rates in France are already below the European average. Yet, when we compare the two countries, this argument hardly holds: the standard VAT rate is at 19% in Germany versus 20% in France. Regarding the reduced VAT rate, it stands at 5.5% and 10% in France (depending on the type of goods) versus 7% in Germany. Overall, the French government seems to have made the strategic choice of favouring targeted transfers to the poorest rather than cutting indirect taxes. After all, disposable incomes in France have so far proved relatively resilient in the crisis (with only a -2.3% q/q decline in Q2), thanks to generous partial unemployment subsidies (EUR31bn) and solidarity fund transfers (EUR7bn).
  In a nutshell, private consumption in France is set for a mechanical rebound, with households being expected to deploy the accumulated EUR100bn (4% GDP) of excess savings in the first half of the year, which coincidentally is roughly equivalent to the French stimulus program.
- ...beyond a focus on curbing unemployment: The French government

estimates that the Covid-19 economic shock will cost around 800,000 jobs by end-2020. However, already in Q2 total job losses (in the private and the public sector combined) exceeded 700,000 while the full partial unemployment scheme was in place. Therefore, by end 2020, we expect total job losses to soar further to nearly 1 million. The government stimulus plan may fall short in addressing the short-term needs as it entails various labor-market measures in an effort to create 160,000 jobs in 2021. The "employment" pillar of the package allocates EUR15.3bn for job protection, vocational training, apprenticeships and hiring subsidies, which require strong adminisrative capabilities to be immediately put into execution. In addition, France is maintaining its furlough scheme for two years under part-time subsidies in sectors severely affected by social distancing requirements such as tourism and art. This means some "zombie" jobs will be maintained for a longer period in France. For other sectors, the partial unemployment scheme will be phased out as of March 2020. We find that the "skill creation" item of the plan is likely to fall short of ensuring a quick reallocation of the jobless between sectors and companies. In view of the existing skill shortcomings and structural rigidities of the French labour market, we expect the unemployment rate to soar up to 12.5% in 2021.

Supply-side measures are at the heart of the French stiumulus.

- Germany's fiscal stimulus does not include much supply-side love. Beyond the financial "bridge support" extended to corporates in the most impacted sectors[1] including hotels, restaurants, bars and clubs for the months of June-August (up to EUR25bn), measures that benefit the corporate sector are hard to find. In addition to the cap on the renewable energy surcharge (EEG surcharge), the *Konjunkturpaket* only includes some limited tax relief and investment incentives, as well as a cap on social security contributions for 2020 for a grand total of EUR13bn (only 10% of the EUR130bn package). Here we see the key shortcoming of the German stimulus package: An opportunity was missed to ease the bureaucratic and fiscal burden for German corporates with a view to boosting investment and job creation. In the short-term, the fiscal stimulus will help provide some "Wumms" to the recovery, but this blatant neglect of the supply side will only allow for a very short-lived impact. Beyond 2022, we don't see any impact on German GDP growth from this package that is worth mentioning.
- Last but not least, Germany is finally promising to invest more with its EUR50bn *Zukunftspaket*. This comes with a focus on health, climate, digital and e-mobility and is coupled with measures to allow for a swift investment, including cutting bureaucracy, fast-tracking projects as well as a simplification of the public procurement law. While we welcome a meaningful investment initiative aimed at modernizing the economy, especially as it is accompanied by measures to speed up implementation, we remain concerned about bottlenecks. Moreover, the *Zukunftspaket* can hardly cover the investment needs of the German economy. Assuming that it is fully implemented, we expect medium-term GDP growth to be lifted by 0.1ppts at the most.

- France's recovery strategy relies essentially on boosting investment

[1] Before introducing the stimulus package in September 2020, the French Government had already introduced during the summer a EUR50 bn support package for the most affected sectors by the Covid-19 economic fallout (e.g. automobile, aerospace, tourism and construction).

rather than stimulating demand, thus the French stimulus package is more ambitious when it comes to dealing with the long-lasting supply-side issues. Under the guise of stimulus to boost competitiveness innovation, the French government aims at pursuing a long-delayed structural reform agenda. France's stimulus package seeks to enhance competitiveness and points at a new strategic direction for the industrial sector over the medium term. The centrepiece of the French stimulus is a EUR20bn production tax cut for French companies over two years. At 9.7% of total value-added, more than double of Germany (4% of value added), this has been hurting the competitiveness of French companies. A EUR10bn reduction in the production tax is expected to increase the net profits of French companies by EUR12.6bn[2] in relation to positive relocalization spillovers. In addition, social charges and record high a corporate tax rate impede profitability of French firms. With the clear purpose of fostering a "made in France" strategy, the government has also maintained its intention of reducing the corporate tax rate to 25% by 2022. The plan also allocates EUR1bn for the "reshoring" of businesses in strategic sectors such as pharmaceuticals and IT.

Who goes greener? Different spending allocations to serve similar ecological goals.

- In a superficial upfront comparison of the stimulus programs, the relative total ambitions and components are similar. In both packages, the share of stimulus measures that can be considered as green amounts to 30%. The German green stimulus is bigger in absolute terms, but the French is slightly larger in relation to GDP. In both packages, the flow of the expected green funds will only materialize over the coming years.
- The funds in the French package, as shown in Figure 1, are fairly balanced between the three categories green mobility, green energy and technologies and renovation of buildings, which make up 78% of the total package. The German stimulus shown in Figure 2 is more focused. Half of the funds are reserved for green energies and technologies. In particular, the funding of a hydrogen economy with EUR9bn considerably larger than the EUR2bn in the French stimulus. At EUR11bn, the green energy support is the single largest part of the German green stimulus. As it is framed in the form of a stabilization of the EEG (Renewable Energy Sources Act) surcharge, it is debatable if it should be included as being green[3]. The French green stimulus lists EUR2.6bn for innovation support for the automobile and aviation industries under the green technology section. It is not clear how far this engagement should be considered green, especially since the description of the measure rather relates to competitiveness issues. A comparable EUR2bn support measure for the German automobile industry has been excluded from the German green stimulus category.
- Another 39% of the German green stimulus is reserved for greening

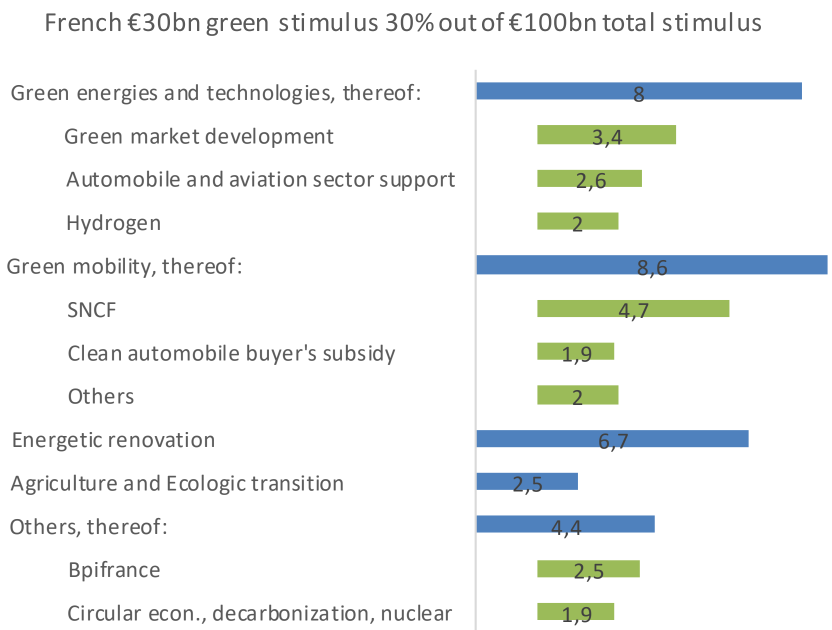
[2] For further information please see https://www.institutmontaigne.org/publications/taxes-de-production-preservons-les-entreprises-dans-les-territoires

[3] After all, the measure aims at freezing the surcharge that is paid by electricity consumers, while an increasing surcharge might seem more climate friendly. This should be seen in the light of the pre-Covid discussion of limiting the EEG surcharge. It should be noted that the EEG surcharge per kWh of electricity that the consumers of electricity pay is different from the feed-in tariffs per kWh of electricity that the producers receive. Only the sum of total surcharges payed and total feed-in tariffs received are equal. Given the same surcharge, the stabilization funds consequently increase the feed-in tariffs for renewable energy installations relative to the alternative of reducing the feed-in tariffs on the renewable electricity production.

transport and mobility. Interestingly, the EUR5bn equity injection for the German railway Deutsche Bahn is in the same ballpark as the EUR4.7bn support for the French railway SNCF. The German plan is more explicit in the distribution of funds to charging station infrastructure (EUR2.5bn) and electric vehicle buyer's subsidies (EUR3.6bn), while the French EUR1.9bn is labelled as a clean vehicle buyer's subsidy, including an unspecified share for extending the charging station network. While the French plan mentions electric and hydrogen vehicles explicitly, it is also open to clean combustion engine cars. It also states a partial conditioning of the bonus on scrapping old vehicles. Past experiences suggest that conditional scrapping is, at least, a questionable policy.

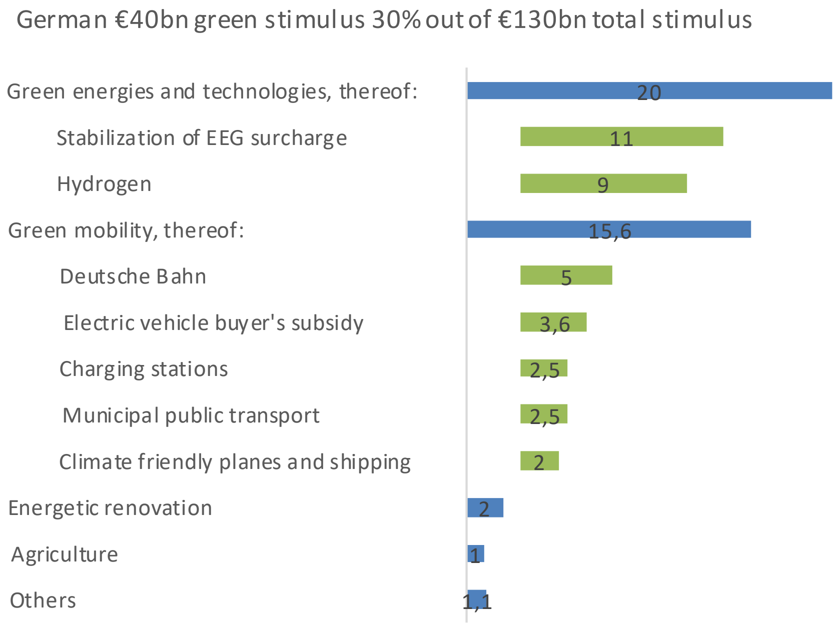
- At EUR2bn, the German funds for green renovation are considerably smaller than the French EUR6.7bn. This seems surprising as energy efficiency gains in buildings are one of the main obstacles for the German energy transition. Still, the utilization and impact of these funds is questionable as the already existing energy renovation programs are unlikely to be fully exploited. Agriculture, forestry and fishing receive only limited attention in the French green stimulus and very limited consideration in the German one. While the French EUR2.5bn includes support on biodiversity, the fight against artificialization, and the ecologic transition of agriculture, forests and fishing, the German EUR1bn only focus on climate resilient forests and improving conditions in animal stables.

Figure 1: Composition of the French green stimulus share



Source: Allianz Research

Figure 2: Composition of the German green stimulus share



Source: Allianz Research

Growth impact

- All in all, the French stimulus largely hinges on complex spending programmes. The EU funding can take some time to materialise while the government expects the take-ups to reach EUR30bn at most in 2021. On the other hand, the German stimulus, with its strong focus on the demand side, is likely to be better at boosting short-term activity. In France, we expect the stimulus package to boost economic growth by +2.4pp between 2020 and 2022. The flipside of this fiscal stimulus will be the widening of the already high trade deficit in France. By stimulating domestic demand, government stimulus packages naturally increase demand for imports, hence benefiting trading partners: out of Europe's major economies, we find that France could experience the largest leakage from its fiscal stimulus (to Germany and Chine), causing its structural merchandise trade deficit to deteriorate by a net –EUR12bn over 2021-22. The picture is radically different in Germany where we estimate the EUR130bn (3.8% of GDP) stimulus to increase economic growth by +2pp between 2020 and 2022. Regarding the import leakage, we expect only a slight decline (of –EUR3bn) because of a lower senstivity of imports to stimulus[4].

[4] For further details please see our publication https://www.allianz.com/en/economic_research/publications/specials_fmo/2020_09_03_fiscalstimulus.html

APPENDIX

The French stimulus plan

The EUR100bn French recovery plan (around 4.3% of 2019 GDP) consists of three pillars: competitiveness and innovation (EUR35bn), ecological and environmental transition; (EUR30bn) and social and territorial cohesion (EUR3bn). Importantly, by focusing on competitiveness, the green transition and human capital, the French plan is in line with the EU's EUR750bn recovery fund requirements agreed in July. Therefore, the French government is counting on an EU contribution of EUR40bn to its stimulus. The French government clearly aspires to relaunch the domestic production engine – even to reshore traditional industries such as automobiles – by addressing the long-lasting structural rigidities of the economy.

Pillar 1: Competitiveness and innovation; EUR34.4 billion

Production tax cuts In 2021, EUR7.25 billion reduction in the corporate value added tax, in addition to a 50% reduction in property taxes for industrial establishments. The measure is expected to benefit to around 32,000 companies, 74% of them being very small and small and medium-sized enterprises.	EUR10 billion in 2021 EUR10 billion in 2022
New investment programme Innovation and investment grants from BPI France (calls for projects) for 2020 and 2021	EUR11 billion
Equity capital for companies Possibility of raising equity participation loans up the EUR10-15 bn thanks to state guarantee. Government is currently seeking an agreement with the banking confederation to lower the cost of these loans.	EUR3 billion
Corporate investment support with particular focus will be on the biotechnology and renewable energy sectors. Calls for projects driven to high-value added production, re-industrialisation and reshoring.	EUR1 billion

Pillar 2: Ecological and environmental transition; EUR30.2 billion

Green mobility EUR4.7 billion for the public railway company SNCF, EUR1.9 billion in subsidies for purchases of clean vehicles and EUR1.2 billion for public transport and urban cycling development and EUR 0.8 billion other measures.	EUR8.6 billion
Green renovation of buildings EUR4 billion for the renovation and insulation of public buildings, EUR2 billion for existing housing (no income conditionality) and EUR500 million for	EUR6.7 billion

a major renovation of the social housing stock and EUR200million for other activities	
Green energy and technology and others: to achieve energy carbon neutrality by 2050 EUR2 billion investment in green hydrogen, EUR3.4 billion in support for green energies, EUR2.6 billion in the aerospace and automotive sectors and EUR200 million in nuclear energy and EUR4.2 billion in other measures	EUR12.4 billion
Agricultural transition: to promote local and sustainable food production Biodiversity and fight against artificialization EUR 1.25 billion, EUR250 million sustainable sea	EUR2.5 billion

Pillar 3: Social and territorial cohesion; EUR35.7 billion

Employment and skills EUR6.7 billion for a **youth plan:** financial assistance, hiring subsidies, civic service for young graduates, apprentices and workers under 26 year old. EUR7.6 billion for the **long-term short time working schemes,** including funding for training, for sectors severely impeded by Covid-19. EUR1 billion investment for skill creation for jobseekers	EUR15.3 billion
Healthcare sector (Ségur plan) Investment in the construction and renovation of hospitals and nursing homes	EUR6 billion
Local government (municipalities) investment and increase in **some social benefits** (EUR500 million for very-high-speed broadband, increase in back-to-school benefits).	EUR5.8 billion
Research & Development Higher education and the French National Research Agency are the main beneficiaries.	EUR0.8billion
Social solidarity EUR100 increase of the annual back to school allocation for low incomes, increased subsidies to university restaurants (EUR600 million) and extra funding (EUR200 million) for associations to help the vulnerable populations.	EUR0.8billion

Germany's fiscal stimulus plan

Measures in Germany's fiscal package	Amount (EUR bn)	Beneficiary
Temporary VAT cut	20	Consumers
Child bonus (EUR300bn per child)	4	Consumers
Cap on social security contributions in 2020	5	Consumers/corporates
EEG surcharge subsidy	11	Consumers/corporates
Purchase incentives for electric vehicles	2	Consumers/corporates
Corporate tax relief	13	Corporates
Financial aid to municipalities & public institutions	13	Municipalities
Zukunftspaket (Investment in health, green energy etc.)	48	
Fast tracking shovel-ready investment projects	10	
Other	3	
Total	**130**	
Additional measures		
Sectoral "bridge support"	25	Corporates
Kurzarbeit	35	Consumers