

# Germany: Chancellor Merkel follows the lead of employers and the FDP

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In her first government statement following re-election as German chancellor, Angela Merkel (Christian Democratic Union, CDU) has made a sharp turn to the right. She has given way to pressure from the pro-market Free Democratic Party (FDP), the big business wing in the CDU and the employers' associations, adopting their demands in her remarks. While forecasting that the population faces difficult times, she announced relief measures for big business and high earners.

At the beginning of her speech, she said it was first necessary to make an "unsparing analysis of the situation of our country," and draw the consequences flowing from it. Merkel has been in office for four years, so the country's "situation" should be well known to her. Talk of an "unsparing analysis" signals the same intention as the oft-repeated "now it's time to pay the bills": It is used to justify the breaking of pre-election promises and to imply there is no alternative to drastic social cuts.

Merkel stressed that "the crisis is far from over," and continued, "The problems will only get bigger before things get better again. The full force of the crisis will hit us next year." By "us," however, she does not mean the better off, but ordinary working people. The economic crisis will hit the jobs market with full force next year, driving up unemployment, with job market experts anticipating a rise of up to 5 million unemployed.

In her statement, Merkel expressly committed herself to tax reforms involving the introduction of new graduated rates in 2011. The introduction of such a system is a core demand of the FDP, while it is disputed inside the CDU and Christian Social Union (CSU). This demand had not been definitively agreed in the coalition agreement between the CDU/CSU and

FDP, which talked about a graduated reform being introduced in 2011 "if possible."

Although Merkel provided no details, the FDP is calling for three graduated tax rates, with a maximum rate of 35 percent. The top rate is currently 42 percent, while 10 years ago it was 53 percent. Reducing the highest tax rate on this scale would mean high earners as a group receiving billions in rebates.

Merkel also acceded to the demands of the FDP in several other regards. Additional mandatory private nursing care insurance is to be introduced, "no matter how much resistance there is," she declared. The health system must be reformed for reasons of "solidarity."

In the coalition agreement, the CDU/CSU and FDP had already agreed to a freeze on health insurance contributions for employers, and to begin the introduction of a flat-rate insurance system not based on income levels. This means an end to the present social insurance scheme paid for equally by employees and employers. In future, employees will have to come up with an increasing proportion of the costs from their own pocket, while the employers' contribution will no longer rise. The introduction of a flat-rate scheme means that the boss will pay just as much for his basic health care as does his chauffeur. The former, however, can also afford to purchase expensive additional insurance, heralding the beginnings of a two-tier health system.

In addition, Merkel announced that the two-year short-time working subsidies introduced by the outgoing grand coalition would be extended beyond the end of 2009. These subsidies have so far prevented a rapid rise in the numbers of unemployed, but have resulted in average incomes clearly sinking. Moreover, pensions are stagnating as a result, since the annual pension increase is calculated against the rise in average

earnings. Meanwhile, the pensions insurance system is assuming there will be no increase in retirement benefits over the next six to seven years. But since pensioners will also have to pay higher health insurance costs, their net income will sink.

Merkel also announced that in future businesses will be able to more easily hire people on limited contracts, increasing the already widespread uncertainty in the jobs market.

The chancellor justified her planned tax reforms with the classic argument of the FDP: lower taxes for business would boost the economy and thus lead to an increase in employment and tax revenues. The state could therefore fulfill its social obligations.

In reality, the tax reductions introduced in recent years have had the opposite effect. The tax breaks landed in the pockets of a tiny layer of the rich and super-rich, while wages and salaries stagnated and state spending and social security benefits were reduced. Growth and upturn predominantly took place on the stock exchanges, where an orgy of speculation finally culminated in the greatest economic crisis in 70 years.

By making the policies of the FDP its own, the new government is boosting this unrestrained enrichment of a few at the expense of the many. Merkel accepts that following this course places her in conflict with a wing of her own party, which has given priority to consolidating the budget before reducing taxes. Several prominent Christian Democrats believe that the FDP's demands cannot be financed. The SPD and Greens are also arguing along the same lines, and are demanding greater budgetary discipline from Merkel.

The new finance minister, Wolfgang Schäuble (CDU), has repeated several times that he intends to ensure new debt is sharply curtailed in this legislative period. That does not mean, however, that he rejects tax cuts for businesses and high earners, but that he will recoup them by cutting social expenditure.

One thing is clear: The government is not going to touch its second largest budget item—servicing the state debt. For 2010, some 41.7 billion euros are earmarked for interest payments to the banks. In the following years this will continue to rise. All the parliamentary parties are agreed that domestic security and defence are also out of bounds as far as budget cuts are concerned. The only expenditure that will be constantly reduced is social spending.

*Süddeutsche Zeitung* commented: “The route is about the future social climate in society. Merkel has now faced up to this duel. Finally.”

Some newspapers described Merkel's rightward swing as rather unusual, based on her previous career. The *Süddeutsche Zeitung* wrote that Merkel's statements at the start of her second period in office mark “a new timetable ... The chancellor no longer wants to engage in the politics of small steps, like four years ago.” The *Frankfurter Rundschau* noted that the “priest's daughter from Templin” wanted “all the hesitation and wavering of the last years to be forgotten,” Merkel, “the eternal appeaser,” was striking the pose of Winston Churchill: blood, sweat, tears.

In reality, Merkel's political biography is characterized by her adaptability. She has always given in to pressure from above; she is only immune to pressure from below.

As early as 2003, at the CDU party congress in Leipzig, she was calling for a fundamental change of course in social and tax policy. At that time, talk was of the “Thatcher-isation of the CDU.” In the 2005 Bundestag (federal parliament) election, the CDU/CSU and FDP failed to gain a majority because she had adopted the demands of economics professor Paul Kirchhof, who advocates the abolition of progressive taxation and the introduction of a “flat-rate” tax system (a uniform tax rate for all).

In the grand coalition with the Social Democratic Party, Merkel left the responsibility for welfare cuts, health reforms and raising the pension age to her social democratic ministers—at least verbally. Now she is returning to the Leipzig party congress line.



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