



# EU Politics: Germany's political impasse spoils EMU reform timeline

- The fluid political situation in Germany threatens to stall EU policymaking in a number of fields, above all the build-out of the euro area. The EU summit on Dec 14/15 is unlikely to yield an agreement on a potential roadmap for reforming the monetary union making it even more difficult to take final decisions in June 2018 as envisaged by the EU Commission. This will in return dampen optimism that a French-German tandem will provide a fresh impetus to the EU as a whole before the European Parliament elections in 2019.
- Mapping out a way forward for the EU27 remains a major issue. A new plan for larger military and security cooperation has been signed recently. In migration policy, however, there is no real progress in finding a joint response to the challenge. Bold EMU reforms are likely to prove difficult, even with a German government in place at some point in 2018.
- Brexit negotiations are unlikely to be impacted immediately. The broad consensus among German parties on this topic allows the German caretaker government to decide with its EU27 partners on whether enough progress has been made to move to the second stage of talks. We regard a positive decision in this respect as likely, clearing the way to negotiate a transition period and guidelines for post-Brexit relations.

*Barbara Boettcher*  
Senior Economist  
(+49) 69 910-31787  
barbara.boettcher@db.com

*Kevin Koerner*  
Economist  
(+49) 69 910-31718  
kevin.koerner@db.com

---

## German elections – the "non-event" of the year

The German elections were supposed to be a non-event in a year with critical national elections across Europe, such as in the Netherlands and France against strong euro-sceptical and populist headwinds. This still holds true in terms of the role and relative importance of populist forces in Germany - even though the right-wing anti-migrant AfD entered the Bundestag. But government formation proved to be way more difficult than expected, resulting in a collapse of coalition talks between the leading CDU/CSU, the Greens and the Liberals – an unprecedented event in Germany's post-war history. At the time of writing momentum was building for a renewed grand coalition between CDU/CSU and SPD to avoid snap elections. Still, this implies a prolonged period of political uncertainty that will last well into spring 2018. From a European perspective, this is a highly unwelcome development at a time when a proactive contribution and guidance from the biggest EU member state is high on demand.

---

## Berlin crucial for ambitious EMU reform timeline

On the top of the EU reform agenda is the build-out of the euro area including a review of institutions and new initiatives for risk-sharing. The EU Commission is expected to put forward more detailed proposals early in December. The agenda should then be discussed in the Eurogroup, allowing EU leaders to endorse a potential roadmap for reforming the euro area at the December 14-15 EU summit (see timeline) and lead to concrete decisions next June. This was



an ambitious timeline in the first place given that proposed reform elements such as a fiscal capacity and a finance minister for the euro area or progress with the common deposit insurance system are highly debated among EMU members. Holding to the planned timeline now seems (even more) unrealistic. The caretaker government under Chancellor Merkel lacks the political legitimacy to take bold decisions and commit Germany to ambitious projects despite a broad pro-European consensus among the mainstream parties and MPs.<sup>1</sup>

The political impasse in Germany has raised concern that the euro area might risk missing a narrow window of (reform) opportunity, undisturbed by the states'/EU election calendar<sup>2</sup> and supported by the current benign economic environment. With lengthy government formation expected in Germany, this window now seems to be shrinking rapidly. The concern is particularly strong in France where President Macron hoped for a strong Franco-German leadership to push through ambitious reforms to European institutions. While Merkel has not subscribed to all of Macron's ideas, she as well as representatives from the CDU already voiced support of the ESM's transformation into a European Monetary Fund, speed up solving legacy issues in the financial sector to fully implement banking union and a review of the overly complex fiscal framework.<sup>3</sup> The general preparedness to strengthen the Franco-German relationship will not be put into question by the current political uncertainty, though. On closer military and security cooperation, another policy field emphasized by Macron in his [Sorbonne speech](#), Germany signed up to a new European defence plan even without a proper government in place.<sup>4</sup> But to find common ground on EMU reforms will be much more difficult, even with a new German government eventually in place early next year. A minimum compromise (extended mandate for ESM/EMF, completing banking/capital markets union) therefore seems to be the most realistic scenario, whereas plans for an EU finance minister and euro area budget including a macroeconomic stabilisation function are at risk of being watered down or discarded.<sup>5</sup>

## Brexit talks – low impact of German political stalemate

For another key topic on the EU agenda – the ongoing Brexit drama - the impact of the political stalemate in Germany should be low. Brexit talks are conducted by the EU Commission under clear "negotiating directives" and guidelines from the EU27. Given that there are no diverging views on content and process of the talks between the major German parties, the acting Chancellor will decide in line with EU27 partners on whether "sufficient progress" has been made on the topics of citizens' rights, fiscal obligations and the border issue in Northern Ireland to move to the second stage of negotiations. Thus, we consider it likely that at the December summit the EU27 will provide the EU Commission with the mandate to start talks on principal orientations for a post-Brexit relationship between the UK and the EU and a possible transition period to get there. Expectations by some observers that Chancellor Merkel by her own would be willing or able to push her partners in the Council towards a more favourable deal for the UK were set to be disappointed in any case.

Figure 1: EU timeline (selected)



Source: Deutsche Bank, European Commission, European Council

1 This consensus would still allow Germany to react to a euro crisis even without a government in place.  
2 No major EU elections between Italian parliamentary elections in early 2018 and European Parliament elections in April/May 2019.  
3 See Focus Europe Special (3 November 2017): "[European integration and the role of the ESM](#)".  
4 See Focus Europe (30 June 2017): "[Defence spending, fiscal stimulus and European integration](#)".  
5 See Focus Europe (9 June 2017): "[EMU reflection paper - mere "wish list" or plausible way forward?](#)".



# Appendix 1

## Important Disclosures

### \*Other information available upon request

\*Prices are current as of the end of the previous trading session unless otherwise indicated and are sourced from local exchanges via Reuters, Bloomberg, and other vendors. Other information is sourced from Deutsche Bank, subject companies, and other sources. For disclosures pertaining to recommendations or estimates made on securities other than the primary subject of this research, please see the most recently published company report or visit our global disclosure look-up page on our website at <http://gm.db.com/ger/disclosure/DisclosureDirectory.eqsr>. Aside from within this report, important conflict disclosures can also be found at <https://gm/db.com/equities> under the "Disclosures Lookup" and "Legal" tabs. Investors are strongly encouraged to review this information before investing.

## Analyst Certification

The views expressed in this report accurately reflect the personal views of the undersigned lead analyst(s). In addition, the undersigned lead analyst(s) has not and will not receive any compensation for providing a specific recommendation or view in this report. Barbara Boettcher, Kevin Koerner, Mark Wall



## Additional Information

The information and opinions in this report were prepared by Deutsche Bank AG or one of its affiliates (collectively "Deutsche Bank"). Though the information herein is believed to be reliable and has been obtained from public sources believed to be reliable, Deutsche Bank makes no representation as to its accuracy or completeness. Hyperlinks to third-party websites in this report are provided for reader convenience only. Deutsche Bank neither endorses the content nor is responsible for the accuracy or security controls of those websites.

If you use the services of Deutsche Bank in connection with a purchase or sale of a security that is discussed in this report, or is included or discussed in another communication (oral or written) from a Deutsche Bank analyst, Deutsche Bank may act as principal for its own account or as agent for another person.

Deutsche Bank may consider this report in deciding to trade as principal. It may also engage in transactions, for its own account or with customers, in a manner inconsistent with the views taken in this research report. Others within Deutsche Bank, including strategists, sales staff and other analysts, may take views that are inconsistent with those taken in this research report. Deutsche Bank issues a variety of research products, including fundamental analysis, equity-linked analysis, quantitative analysis and trade ideas. Recommendations contained in one type of communication may differ from recommendations contained in others, whether as a result of differing time horizons, methodologies, perspectives or otherwise. Deutsche Bank and/or its affiliates may also be holding debt or equity securities of the issuers it writes on. Analysts are paid in part based on the profitability of Deutsche Bank AG and its affiliates, which includes investment banking, trading and principal trading revenues.

Opinions, estimates and projections constitute the current judgment of the author as of the date of this report. They do not necessarily reflect the opinions of Deutsche Bank and are subject to change without notice. Deutsche Bank provides liquidity for buyers and sellers of securities issued by the companies it covers. Deutsche Bank research analysts sometimes have shorter-term trade ideas that may be inconsistent with Deutsche Bank's existing longer-term ratings. Trade ideas for equities can be found at the SOLAR link at <http://gm.db.com>. A SOLAR idea represents a high-conviction belief by an analyst that a stock will outperform or underperform the market and/or a specified sector over a time frame of no less than two weeks and no more than six months. In addition to SOLAR ideas, analysts may occasionally discuss with our clients, and with Deutsche Bank salespersons and traders, trading strategies or ideas that reference catalysts or events that may have a near-term or medium-term impact on the market price of the securities discussed in this report, which impact may be directionally counter to the analysts' current 12-month view of total return or investment return as described herein. Deutsche Bank has no obligation to update, modify or amend this report or to otherwise notify a recipient thereof if an opinion, forecast or estimate changes or becomes inaccurate. Coverage and the frequency of changes in market conditions and in both general and company-specific economic prospects make it difficult to update research at defined intervals. Updates are at the sole discretion of the coverage analyst or of the Research Department Management, and the majority of reports are published at irregular intervals. This report is provided for informational purposes only and does not take into account the particular investment objectives, financial situations, or needs of individual clients. It is not an offer or a solicitation of an offer to buy or sell any financial instruments or to participate in any particular trading strategy. Target prices are inherently imprecise and a product of the analyst's judgment. The financial instruments discussed in this report may not be suitable for all investors, and investors must make their own informed investment decisions. Prices and availability of financial instruments are subject to change without notice, and investment transactions can lead to losses as a result of price fluctuations and other factors. If a financial instrument is denominated in a currency other than an investor's currency, a change in exchange rates may adversely affect the investment. Past performance is not necessarily indicative of future results. Performance calculations exclude transaction costs, unless otherwise indicated. Unless otherwise indicated, prices are current as of the end of the previous trading session and are sourced from local exchanges via Reuters, Bloomberg and other vendors. Data is also sourced from Deutsche Bank, subject companies, and other parties.

The Deutsche Bank Research Department is independent of other business divisions of the Bank. Details regarding organizational arrangements and information barriers we have established to prevent and avoid conflicts of interest with respect to our research are available on our website under Disclaimer, found on the Legal tab.



Macroeconomic fluctuations often account for most of the risks associated with exposures to instruments that promise to pay fixed or variable interest rates. For an investor who is long fixed-rate instruments (thus receiving these cash flows), increases in interest rates naturally lift the discount factors applied to the expected cash flows and thus cause a loss. The longer the maturity of a certain cash flow and the higher the move in the discount factor, the higher will be the loss. Upside surprises in inflation, fiscal funding needs, and FX depreciation rates are among the most common adverse macroeconomic shocks to receivers. But counterparty exposure, issuer creditworthiness, client segmentation, regulation (including changes in assets holding limits for different types of investors), changes in tax policies, currency convertibility (which may constrain currency conversion, repatriation of profits and/or liquidation of positions), and settlement issues related to local clearing houses are also important risk factors. The sensitivity of fixed-income instruments to macroeconomic shocks may be mitigated by indexing the contracted cash flows to inflation, to FX depreciation, or to specified interest rates – these are common in emerging markets. The index fixings may – by construction – lag or mis-measure the actual move in the underlying variables they are intended to track. The choice of the proper fixing (or metric) is particularly important in swaps markets, where floating coupon rates (i.e., coupons indexed to a typically short-dated interest rate reference index) are exchanged for fixed coupons. Funding in a currency that differs from the currency in which coupons are denominated carries FX risk. Options on swaps (swaptions) the risks typical to options in addition to the risks related to rates movements.

Derivative transactions involve numerous risks including market, counterparty default and illiquidity risk. The appropriateness of these products for use by investors depends on the investors' own circumstances, including their tax position, their regulatory environment and the nature of their other assets and liabilities; as such, investors should take expert legal and financial advice before entering into any transaction similar to or inspired by the contents of this publication. The risk of loss in futures trading and options, foreign or domestic, can be substantial. As a result of the high degree of leverage obtainable in futures and options trading, losses may be incurred that are greater than the amount of funds initially deposited – up to theoretically unlimited losses. Trading in options involves risk and is not suitable for all investors. Prior to buying or selling an option, investors must review the "Characteristics and Risks of Standardized Options", at <http://www.optionsclearing.com/about/publications/character-risks.jsp>. If you are unable to access the website, please contact your Deutsche Bank representative for a copy of this important document.

Participants in foreign exchange transactions may incur risks arising from several factors, including: (i) exchange rates can be volatile and are subject to large fluctuations; (ii) the value of currencies may be affected by numerous market factors, including world and national economic, political and regulatory events, events in equity and debt markets and changes in interest rates; and (iii) currencies may be subject to devaluation or government-imposed exchange controls, which could affect the value of the currency. Investors in securities such as ADRs, whose values are affected by the currency of an underlying security, effectively assume currency risk.

Deutsche Bank is not acting as a financial adviser, consultant or fiduciary to you or any of your agents with respect to any information provided in this report. Deutsche Bank does not provide investment, legal, tax or accounting advice, and is not acting as an impartial adviser. Information contained herein is being provided on the basis that the recipient will make an independent assessment of the merits of any investment decision, and is not meant for retirement accounts or for any specific person or account type. The information we provide is directed only to persons we believe to be financially sophisticated, who are capable of evaluating investment risks independently, both in general and with regard to particular transactions and investment strategies, and who understand that Deutsche Bank has financial interests in the offering of its products and services. If this is not the case, or if you or your agent are an IRA or other retail investor receiving this directly from us, we ask that you inform us immediately.

Unless governing law provides otherwise, all transactions should be executed through the Deutsche Bank entity in the investor's home jurisdiction. Aside from within this report, important risk and conflict disclosures can also be found at <https://gm.db.com> on each company ' s research page and under the "Disclosures Lookup" and "Legal" tabs. Investors are strongly encouraged to review this information before investing.

**United States:** Approved and/or distributed by Deutsche Bank Securities Incorporated, a member of FINRA, NFA and SIPC. Analysts located outside of the United States are employed by non-US affiliates that are not subject to FINRA regulations, including those regarding contacts with issuer companies.



**Germany:** Approved and/or distributed by Deutsche Bank AG, a joint stock corporation with limited liability incorporated in the Federal Republic of Germany with its principal office in Frankfurt am Main. Deutsche Bank AG is authorized under German Banking Law and is subject to supervision by the European Central Bank and by BaFin, Germany ' s Federal Financial Supervisory Authority.

**United Kingdom:** Approved and/or distributed by Deutsche Bank AG acting through its London Branch at Winchester House, 1 Great Winchester Street, London EC2N 2DB. Deutsche Bank AG in the United Kingdom is authorised by the Prudential Regulation Authority and is subject to limited regulation by the Prudential Regulation Authority and Financial Conduct Authority. Details about the extent of our authorisation and regulation are available on request.

**Hong Kong:** Distributed by Deutsche Bank AG, Hong Kong Branch or Deutsche Securities Asia Limited.

**India:** Prepared by Deutsche Equities India Private Limited (DEIPL) having CIN: U65990MH2002PTC137431 and registered office at 14th Floor, The Capital, C-70, G Block, Bandra Kurla Complex Mumbai (India) 400051. Tel: + 91 22 7180 4444. It is registered by the Securities and Exchange Board of India (SEBI) as a Stock broker bearing registration nos.: NSE (Capital Market Segment) - INB231196834, NSE (F&O Segment) INF231196834, NSE (Currency Derivatives Segment) INE231196834, BSE (Capital Market Segment) INB011196830; Merchant Banker bearing SEBI Registration no.: INM000010833 and Research Analyst bearing SEBI Registration no.: INH000001741. DEIPL may have received administrative warnings from the SEBI for breaches of Indian regulations. Deutsche Bank and/or its affiliate(s) may have debt holdings or positions in the subject company. With regard to information on associates, please refer to the "Shareholdings" section in the Annual Report at: <https://www.db.com/ir/en/annual-reports.htm>.

**Japan:** Approved and/or distributed by Deutsche Securities Inc.(DSI). Registration number - Registered as a financial instruments dealer by the Head of the Kanto Local Finance Bureau (Kinsho) No. 117. Member of associations: JSDA, Type II Financial Instruments Firms Association and The Financial Futures Association of Japan. Commissions and risks involved in stock transactions - for stock transactions, we charge stock commissions and consumption tax by multiplying the transaction amount by the commission rate agreed with each customer. Stock transactions can lead to losses as a result of share price fluctuations and other factors. Transactions in foreign stocks can lead to additional losses stemming from foreign exchange fluctuations. We may also charge commissions and fees for certain categories of investment advice, products and services. Recommended investment strategies, products and services carry the risk of losses to principal and other losses as a result of changes in market and/or economic trends, and/or fluctuations in market value. Before deciding on the purchase of financial products and/or services, customers should carefully read the relevant disclosures, prospectuses and other documentation. "Moody's", "Standard & Poor's", and "Fitch" mentioned in this report are not registered credit rating agencies in Japan unless Japan or "Nippon" is specifically designated in the name of the entity. Reports on Japanese listed companies not written by analysts of DSI are written by Deutsche Bank Group's analysts with the coverage companies specified by DSI. Some of the foreign securities stated on this report are not disclosed according to the Financial Instruments and Exchange Law of Japan. Target prices set by Deutsche Bank's equity analysts are based on a 12-month forecast period..

**Korea:** Distributed by Deutsche Securities Korea Co.

**South Africa:** Deutsche Bank AG Johannesburg is incorporated in the Federal Republic of Germany (Branch Register Number in South Africa: 1998/003298/10).

**Singapore:** This report is issued by Deutsche Bank AG, Singapore Branch or Deutsche Securities Asia Limited, Singapore Branch (One Raffles Quay #18-00 South Tower Singapore 048583, +65 6423 8001), which may be contacted in respect of any matters arising from, or in connection with, this report. Where this report is issued or promulgated by Deutsche Bank in Singapore to a person who is not an accredited investor, expert investor or institutional investor (as defined in the applicable Singapore laws and regulations), they accept legal responsibility to such person for its contents.

**Taiwan:** Information on securities/investments that trade in Taiwan is for your reference only. Readers should independently evaluate investment risks and are solely responsible for their investment decisions. Deutsche Bank research may not be distributed to the Taiwan public media or quoted or used by the Taiwan public media without written consent. Information on securities/instruments that do not trade in Taiwan is for informational purposes only and is not to be



construed as a recommendation to trade in such securities/instruments. Deutsche Securities Asia Limited, Taipei Branch may not execute transactions for clients in these securities/instruments.

**Qatar:** Deutsche Bank AG in the Qatar Financial Centre (registered no. 00032) is regulated by the Qatar Financial Centre Regulatory Authority. Deutsche Bank AG - QFC Branch may undertake only the financial services activities that fall within the scope of its existing QFCRA license. Its principal place of business in the QFC: Qatar Financial Centre, Tower, West Bay, Level 5, PO Box 14928, Doha, Qatar. This information has been distributed by Deutsche Bank AG. Related financial products or services are only available only to Business Customers, as defined by the Qatar Financial Centre Regulatory Authority.

**Russia:** The information, interpretation and opinions submitted herein are not in the context of, and do not constitute, any appraisal or evaluation activity requiring a license in the Russian Federation.

**Kingdom of Saudi Arabia:** Deutsche Securities Saudi Arabia LLC Company (registered no. 07073-37) is regulated by the Capital Market Authority. Deutsche Securities Saudi Arabia may undertake only the financial services activities that fall within the scope of its existing CMA license. Its principal place of business in Saudi Arabia: King Fahad Road, Al Olaya District, P.O. Box 301809, Faisaliah Tower - 17th Floor, 11372 Riyadh, Saudi Arabia.

**United Arab Emirates:** Deutsche Bank AG in the Dubai International Financial Centre (registered no. 00045) is regulated by the Dubai Financial Services Authority. Deutsche Bank AG - DIFC Branch may undertake only the financial services activities that fall within the scope of its existing DFSA license. Its principal place of business in the DIFC: Dubai International Financial Centre, The Gate Village, Building 5, PO Box 504902, Dubai, U.A.E. This information has been distributed by Deutsche Bank AG. Related financial products or services are available only to Professional Clients, as defined by the Dubai Financial Services Authority.

**Australia:** Retail clients should obtain a copy of a Product Disclosure Statement (PDS) relating to any financial product referred to in this report and consider the PDS before making any decision about whether to acquire the product. Please refer to Australia-specific research disclosures and related information at <https://australia.db.com/australia/content/research-information.html>

**Australia and New Zealand:** This research is intended only for "wholesale clients" within the meaning of the Australian Corporations Act and New Zealand Financial Advisors Act, respectively.

Additional information relative to securities, other financial products or issuers discussed in this report is available upon request. This report may not be reproduced, distributed or published without Deutsche Bank's prior written consent. Copyright © 2017 Deutsche Bank AG



---

## David Folkerts-Landau

Group Chief Economist and Global Head of Research

Raj Hindocha  
Global Chief Operating Officer  
Research

Michael Spencer  
Head of APAC Research  
Global Head of Economics

Steve Pollard  
Head of Americas Research  
Global Head of Equity Research

Anthony Klarman  
Global Head of  
Debt Research

Paul Reynolds  
Head of EMEA  
Equity Research

Dave Clark  
Head of APAC  
Equity Research

Pam Finelli  
Global Head of  
Equity Derivatives Research

Andreas Neubauer  
Head of Research - Germany

Spyros Mesomeris  
Global Head of Quantitative  
and QIS Research

---

### International locations

#### Deutsche Bank AG

Deutsche Bank Place  
Level 16  
Corner of Hunter & Phillip Streets  
Sydney, NSW 2000  
Australia  
Tel: (61) 2 8258 1234

#### Deutsche Bank AG

Mainzer Landstrasse 11-17  
60329 Frankfurt am Main  
Germany  
Tel: (49) 69 910 00

#### Deutsche Bank AG

Filiale Hongkong  
International Commerce Centre,  
1 Austin Road West, Kowloon,  
Hong Kong  
Tel: (852) 2203 8888

#### Deutsche Securities Inc.

2-11-1 Nagatacho  
Sanno Park Tower  
Chiyoda-ku, Tokyo 100-6171  
Japan  
Tel: (81) 3 5156 6770

#### Deutsche Bank AG London

1 Great Winchester Street  
London EC2N 2EQ  
United Kingdom  
Tel: (44) 20 7545 8000

#### Deutsche Bank Securities Inc.

60 Wall Street  
New York, NY 10005  
United States of America  
Tel: (1) 212 250 2500

---