



## What Jamaica has to do with German Energy Policies

*On the 24<sup>th</sup> of September 2017 are general elections in Germany. Admittedly, party programs are vague at best. Some suggestions and ideas found in the party programs may, however, have significant consequences for the German power market and neighbouring countries, including the Nordic countries. While it is likely that Merkel will lead the coming government, it is uncertain what coalition options she may have. Depending on the coalition options, the one or other surprise in German energy policy may be on the horizon, yet again.*

Angela Merkel has shaped German energy policies more than any other chancellor before her. Indeed, the name Energiewende is now mostly associated with Angela Merkel, while it was actually the Red-Green government under Chancellor Schröder that laid foundation for the Erneuerbaren Energie Gesetz (EEG) as we know it. It was also Angela Merkel who, after the Fukushima nuclear accident, decided to decommission older nuclear plants from one day to the other, and re-confirmed the nuclear exit strategy that the Schröder government originally implemented (and that she first declared void).

Looking at the current opinion polls for Germany, it is likely that Merkel will also lead the coming government in Germany. The campaign of her opponent, Social Democrat Martin Schulz, lost momentum. Current polls suggest some 38%-40% for the Christian Democrats under Merkel, while the Social Democrats under Schulz may only expect something between 23%-24% of the votes. When asked for who should govern Germany's next government, the gap is even larger. 60% prefer Merkel, while only 30% name Schulz as the preferred next chancellor.

### Many coalition options

However, neither party has an absolute majority, and hence depend on coalition partners to form a coalition (see Figure 1 for latest polls). This is in fact Schulz' only hope for becoming chancellor of the next German government. Together with *Die Grünen* (Green Party) and *Die Linke* (The Left Party), he may expect in total some 41% of the votes. Yet, as this is still far from a majority, it is unlikely that this will suffice on the 24<sup>th</sup> of September.

In short, Merkel is the most likely winner for the coming election. Coalition options are in fact tricky and are at the moment highly uncertain, partly due to the rise of populist-right party *Alternative für Deutschland* (Alternative for Germany). All major parties said clearly that a collation with the Alternative for Germany, currently polling at around 8%, is out of question.

A continuation of the current grand coalition of Christian Democrats and Social Democrats would certainly have a majority

in the *Bundestag* (the German Parliament), but for many reasons it is also the least preferred option for many. Arguments against this option include the lack of a strong opposition, a too strong focus on consensus, and Social Democrats being in the shadow under Merkel and being marginalized.

Another option is a coalition between Christian Democrats and the Liberals, who can expect to re-enter the Parliament after they startlingly failed to do so four years ago. However, the two parties, currently polling at between 46%-48% of the votes, may not have a majority. The Greens can currently expect something in the same magnitude as the Liberals (8%), and hence a coalition between Christian Democrats and Greens is also likely to be short of a majority.

Some argue therefore for what is called a "Jamaica" coalition, consisting of the Christian Democrats (associated with color black), the Liberals (yellow), and the Greens (green). This coalition could indeed gain a comfortable majority.

Figure 1: Current Polls for the coming German General Election

	Allensbach	Emnid	Forsa	Forsch'gr.	GMS	Infratest	INSA
CDU/CSU	40 %	39 %	39 %	40 %	40 %	39 %	38 %
SPD	25 %	24 %	23 %	24 %	22 %	24 %	24 %
GRÜNE	7 %	8 %	8 %	8 %	8 %	8 %	7 %
FDP	9 %	8 %	8 %	8 %	9 %	8 %	9 %
DIE LINKE	9 %	9 %	9 %	8 %	8 %	9 %	9 %
AFD	7 %	7 %	8 %	8 %	7 %	8 %	10 %
Other	4 %	5 %	5 %	4 %	6 %	4 %	3 %

### Party programs are vague

It would be out of scope for this Insight letter to discuss the party programs and their relevance for energy policy in detail. In addition, party programs are in large parts very vague, making drawing concrete conclusions very difficult. There are nevertheless some interesting points in the respective party programs that deserve further commenting:

- *Christian Democrats*: They are rejecting state intervention in the EU-ETS market (as for example carbon price floors), and focus on market based instruments. They aim to keep Germany in one bidding zone.

- **Social Democrats:** They still have a focus on promoting renewable energies (by which they supposedly also mean subsidies). They want to develop the EU-ETS as a central instrument for climate protection, but may consider a price floor should the EU-ETS not work as intended.
- **Liberals:** They consider the EEG as obsolete, consider renewables as competitive, and would like to abolish the current EEG. Instead of allowing introducing a price floor for carbon, they rather want to extend the EU-ETS to other sectors.
- **Green Party:** They propagate a price floor for the EU-ETS and a deletion of the EUA surplus. In addition, they want to mothball the “20 dirtiest coal power plants” and have a 100% renewable power sector by 2030. The mothballing of old coal plants is, according to some, even a pre-condition for the Greens to join a coalition.

As a participation of the Left party and the Alternative for Germany seems rather unlikely, we are not discussing their policies here.

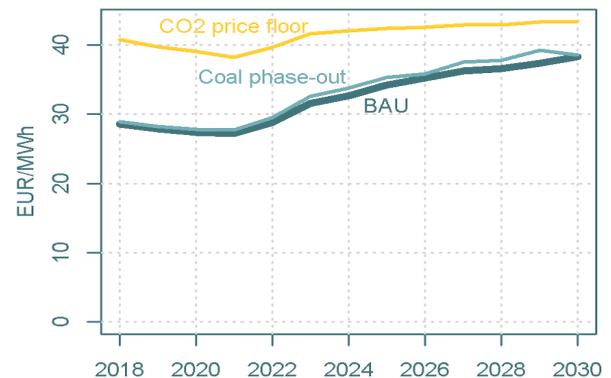
### Everything else than Grand Coalition could imply surprises

Looking at the potential coalitions, this means that Germany could yet again surprise its citizens and its neighbors with a revised energy policy. Admittedly, the Liberals and the Green Party are far away from each other. But the Liberals may yield in the field of energy policy, if they gain grounds on other political fields, like general economic policies and policies for interior affairs.

In particular, two options deserve further investigation: the impact of a carbon price floor in Germany, and the impact of an accelerated coal phase out. We have therefore simulated the German power market with 1) a coal phase out according to a track published by Agora Energiewende, and with 2) a scenario in which Germany introduces unilaterally a carbon price floor of EUR 30 per MWh. This level is in the magnitude of the floor suggested in France (plans which may indeed be revitalized by President Macron) and in the magnitude of the current effective carbon price in Great Britain.

The results from our simulations are shown in the Figure 2 below. Power prices are not reacting very strongly to an accelerated coal phase-out. Already today, many coal plants are about to be decommissioned or mothballed, and the majority of additional phase-out outlined by Agora is post 2025. In addition, there are as of today large excess capacities, and in particular gas capacities are under-utilized. And, after the nuclear phase-out in 2022 in Germany, it is anyway mostly gas that is the marginal price setter, not coal. While the spot market consequences are limited, it is needless to say that effects for utilities, however, could be severe, in particular if some of the highly profitable lignite plants are affected.

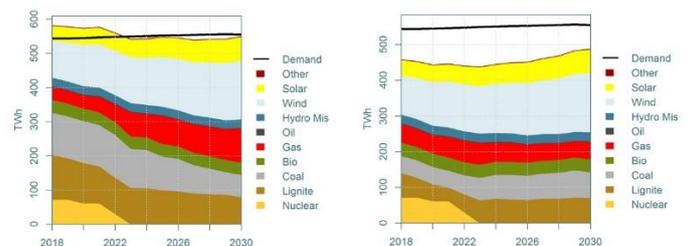
Figure 2: Power prices in Germany under an accelerated coal phase-out and a carbon price floor, together with a Business as Usual (BAU) case



The effects of a unilateral carbon price floor, however, are much more significant. As the carbon price feeds directly into the short-run marginal costs of gas and coal fired plants, prices would rise substantially. While this would reduce the carbon intensity of the German power market, Germany would become a substantial net importer, as power prices in the surrounding countries would be much smaller, outcompeting German generation (see Figure 3).

In fact, a German carbon price floor would also reduce emissions on a European level, even more so than an accelerated coal phase out. But the problem with such unilateral measures is that they would undermine the EU-ETS even further, unless this is combined with a substantial reform of the EU-ETS (see also the TCG-Insight 2015-10 “It is time for reform of the EU ETS, not for national measures”).

Figure 3: Generation mix in Germany (left = accelerated coal phase-out; right = carbon price floor)



It is, of course, too early to predict both the next coalition in Germany, and what policies certain parties may push through. But it may in fact be that there are some surprises looming on the horizon. And, due to its importance for the European power markets and the prices also in the Nordic region, this may also have severe price consequences for the Nordic countries. Time will tell.

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