

Germany's Budget Compromise: Cutting Corners is a Losing Strategy

The Ampel coalition's dismal prospects for reelection next year have bred desperation. Their recent budget compromise does not just make funding defense a challenge for the next government, but it also keeps hollowing out key political tools to promote Germany's core interests and commitments abroad.

Explainer by Philipp Rotmann

July 2024

After tough negotiations, Germany's governing coalition has landed on a compromise for the 2025 draft budget it will submit to parliament. The Social Democrats (SPD) and Greens managed to protect their core priorities. In return, they had to allow their coalition partner, the fiscally hyper-conservative Free Democrats (FDP), led by Finance Minister Christian Lindner, to claim overall savings compared to this year's budget. But these savings are minimal, as economists Florian Schuster, Felix Heilmann, Vitus Rennert, and Philippa Sigl-Glöckner [have shown](#).

The result is a strategically short-sighted budget proposal. On top of massive reductions last year, this federal budget will again cut Germany's contribution to humanitarian assistance and crisis management by half (-47 percent), to save 0.26 percent of the budget. The development ministry's reconstruction aid is to be slashed by a third (-35 percent) and its food aid by half (-52 percent), for another 0.08 percent in budgetary savings. Combined with other cuts and exceptionally hopeful assumptions, the government will be saving 0.2 percent of the country's expected gross domestic product of €4.4 trillion, with a quarter of that (0.05 percent) coming out of foreign affairs and aid. And still the Bundestag is being asked to sign defense procurement contracts without having set aside the money needed to fulfill them.

The defense component is not difficult to explain: it is impossible to rearm at scale without raising taxes, increasing debt or slashing social services, but the Ampel coalition decided to have it both ways. They will place the orders and leave it to the next government to pay, basically. The downsides of this approach are clear – you do not win the trust of partners or the respect of adversaries with such maneuvers, and defense contractors will find ways to slip risk premiums into their contracts that make them even more expensive for the German taxpayer. Still, this choice may have been politically unavoidable for a coalition of fiscal hawks and center-left progressives suddenly confronted with a historic requirement to start rapidly rebuilding their hollowed-out Bundeswehr.

The bigger surprise is that the same government that proclaimed the *Zeitenwende* – a “watershed moment” that requires “investing in strength” – has decided to slash key tools for defending its international interests. Not just a little, but by about half. In terms of budget discipline, these savings are purely cosmetic; in strategic terms, they come with a massive, if delayed, cost. So why is this happening? Why would the consequences be so severe? What are the flaws in the coalition's reasoning? And what does all this have to do with next year's general election?

Where Is This Coming From?

In December 2021, the Free Democrats came into government as the smallest coalition partner. On the campaign trail and when taking office, they loudly portrayed themselves as the hardest-nosed realists when it came to foreign and security policy, while sticking to their signature fiscal conservatism. They were the sole party to propose spending not just 2 percent of GDP on defense, which is NATO's target for members, but 3 percent. As Lindner suggested, this outlay would be “for defense, but also for diplomacy and development as crisis prevention measures.”

This figure was widely deemed unrealistic at the time: real spending for defense, diplomacy and development hovered around 1.5 percent of GDP. But the Free Democrats drove a hard bargain when forming a government with the left-leaning SPD and Greens. They insisted on their security investment quota as a goal for the coalition – and on FDP control of the Ministry of Finance. The coalition agreement held that all this new money would be found within the budget and the tight limitations of the constitutional “debt brake,” the mechanism that restricts government borrowing.

Russia's full-scale invasion of Ukraine in February 2022 at first appeared to bring major change to German politics. The government drafted the country's first-ever National Security Strategy amid unprecedented decisions to send high-tech weapons systems to an active war and create a €100 billion special fund for the Bundeswehr. In a landmark speech on February 27, 2022, Chancellor Olaf Scholz (SPD) spoke of the *Zeitenwende* while framing the stakes of what was to come. The key question, Scholz said, “is whether power is allowed to prevail over the law... or whether we have it in us to keep warmongers like Putin in check. That requires strength of our own.”

Scholz recognized that rebuilding this strength would not be cost-free. Protecting Germany's freedom and democracy – through “a powerful, cutting-edge, progressive Bundeswehr that can be relied upon to protect us” – would be “a major national undertaking.” Scholz continued: “We should be under no illusions. Better equipment, modern technology, more personnel – all of this costs a lot of money.” Germany was to begin rebuilding this strength through the special fund, likely to be spent quickly, and a renewed commitment to hit the 2 percent defense spending target “every year” onward. Scholz received the full support of the Free Democrats and their leader in the Finance Ministry.

Fast forward to June 2023, when the time came to adopt the National Security Strategy: Lindner insisted on sticking to his fiscal red line from the coalition agreement. Every euro spent beyond the short-lived special fund would need to come out of savings elsewhere in the budget. From the start, this hard line singlehandedly dragged down the Bundeswehr's combat readiness: every new tank, ship or plane purchased through the special fund needs fuel, spare parts and ammunition – paid for out of the regular budget.

Meanwhile, the FDP's historic electoral success in 2021 – a 11.5 percent vote share, the party's second-best result since 1961 – had given way to a steady decline. By the fall of 2023, Lindner's party was polling close to the 5 percent threshold needed to enter the next parliament. According to party insiders, this put the FDP on the brink of disaster; the combination of competition for the center-right vote, financial troubles and internal ideological diversity is still seen as an existential risk for the party.

Lindner has one last full budget cycle to galvanize his base before the next election. In the eyes of its chairman, the FDP's survival depends on maintaining its image as the last defender of budgetary restraint amid free-spending lefties. Every government program that is not at

the heart of their voters' most immediate personal interests must therefore be fair game. While the FDP would have loved to go after social spending, the SPD and Greens predictably met any such calls with fierce resistance. Which left whatever could be squeezed out of foreign affairs and development budgets – a relatively small share that will mainly come at the expense of humanitarian aid and crisis management.

According to polls, aid is indeed the first thing the German electorate would choose to cut if its government were short on money. This might explain the public messaging. Except that what has been portrayed as going after “foreign aid” would in fact be a massive blow to key sources of Germany's trust and influence abroad – and thus to a major component of German and European security. To see why, a closer look at the proposed cuts is required.

What Would Be the Consequences?

To be realistic, a nod to populist impulses only partly explains why the cuts have so disproportionately hit aid budgets. They are also about the only pieces of the Foreign Office and Development Ministry's budgets that can be easily changed.

Svenja Schulze (SPD), the head of the Development Ministry (BMZ), has a large part of her budget tied up in long-term formal agreements with international organizations and recipient governments. The spending that remains discretionary largely goes to crisis response and climate adaptation – in other words, short-term support to help crisis-affected people provide for themselves in the wake of disaster, and investments to fight the climate crisis abroad.

The cuts to the BMZ's crisis response tools alone amount to €395 million. This means less support for Syrian refugees in Jordan and Lebanon, and for the displaced and war-affected populations in the Sahel and across the Horn of Africa. In addition to classical development aid through the European Development Fund, Germany's international investments in CO2 reductions – 80 percent of which are managed by the BMZ – would be the other big victim to the tune of €100 million in cuts. A rollback on this front would prevent Germany from fighting the climate crisis where it is cheapest to do so. Because labor and raw materials cost less in developing countries, the same number of euros can prevent many more tons of CO² emissions there than compared to Germany.

On the Foreign Office side, Foreign Minister Annalena Baerbock (Greens) appears to have successfully resisted the worst of the expected cuts after having already accepted substantial cuts for this year. But still, the budget draft requires her ministry to save another 27 percent on “securing peace and stability,” the heading that covers humanitarian aid, crisis management and climate action. Since 2023, the start of the austerity measures, the Finance Ministry's demands add up to a cumulative 39 percent struck from this heading. This means more than €1.6 *billion* would be pulled from quick fixes (humanitarian aid) as well as efforts to prevent and recover from war (crisis management and stabilization) between 2023 and 2025. These are small sums compared to defense or welfare budgets, yet they are still crucial components of German foreign policy in a world with plenty of death and destruction whose consequences are directly hitting export-dependent Germany.

Making these cuts will have grave strategic consequences. Only two years ago, this same coalition promised anxious governments in Africa, Asia and Latin America that its support for Ukraine would not come at the expense of aid. In view of the global food crisis triggered by the loss of Ukrainian grain exports, and the lingering resentment over how rich countries slow-walked COVID vaccine distribution, this promise was central for preserving majorities

within the United Nations to uphold the principles of international law – and condemn Russia’s war of aggression alongside Western countries.

In comparing German spending to others, it does not help to whine about double standards. Yes, being the No. 2 global provider of emergency aid as the fourth-largest economy means that others are not playing their part. But Germans, for many years, were happy to be paying far less than the 2 percent NATO target for defense. Whether Germany’s relative humanitarian generosity is “fair” compared to the Gulf monarchies, for example, is irrelevant. Humanitarian aid to save Palestinian lives is currently Germany’s only substantive answer to the charge of uncritical support for a militant right-wing government in Israel. So, the key question to ask about aid is this: can Germany afford to be widely seen as abdicating its basic responsibilities as a rich country?

If a loss of soft power seems trivial as hard power returns to the forefront of geopolitics, think again: this would be a dangerous misreading of Germany’s position in the world. Germany’s hard power position is dismal and will take many years to improve. As China and other middle-income countries supply ever more cars, railways and power stations, the developing world’s technological dependency on the West is waning. Germany’s economy and population can no longer count on the unearned advantages that accrued from these relationships, and from sailing in the wake of the United States, France and the United Kingdom – especially as Washington continues to withdraw from Europe, regardless of the election result in November.

As a result, it will take more for Germany to maintain its influence than it did a decade or two ago. The massive increases in those aid budgets over the last 20 years were neither an accident nor the result of fiscal abundance; they were a shrewd strategic investment that the current austerity trend is at risk of sabotaging. And once lost, trust and influence are all the more expensive to regain.

Flawed Justification or Wishful Thinking?

How, then, does the government justify gutting its international influence? Lindner argues, and both Chancellor Scholz and Vice-Chancellor Robert Habeck (Greens) appear to have accepted, that the country’s international spending needs to return to the so-called “pre-crisis levels” of 2017 to 2019. That is both wishful thinking and plainly misleading.

While the darkest days of the COVID pandemic are indeed over, wars continue to rage. Defending Europe in Ukraine has required massive outlays: Scholz recently cited a figure of €28 billion in military aid alone. That is more than half of Germany’s pre-war defense budget, or *four times the entire budget of the Foreign Office* – which managed several hundred million euros of humanitarian and stabilization support for Ukraine through various emergency channels. The financial implications of Israel’s war on Gaza have so far solely hit humanitarian aid, but Berlin is expected to contribute to reconstruction and perhaps security in the coming years. Then there is the war in Sudan, just one of the many other crises completely overlooked in Germany.

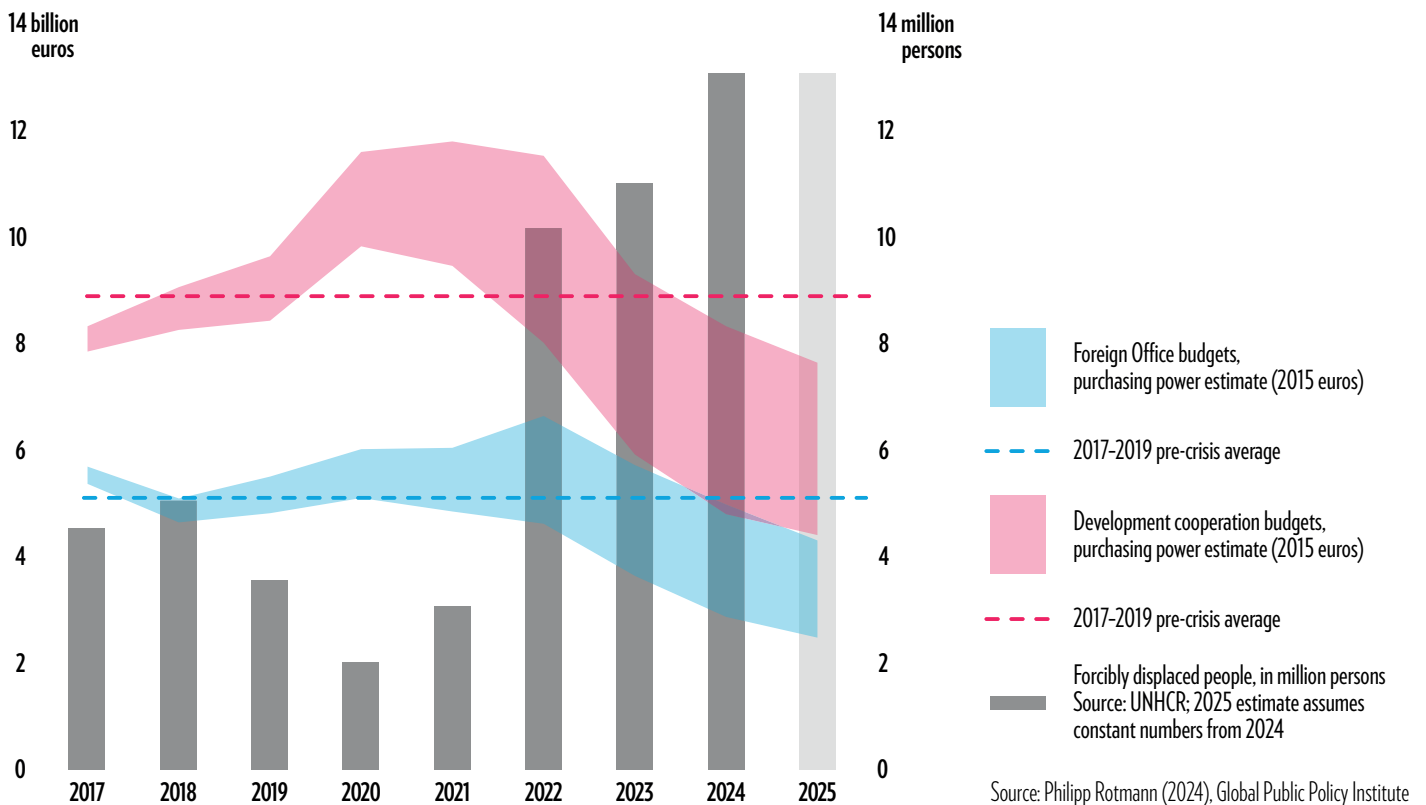
As a rough benchmark for current trends, consider that the number of wars and the number of people displaced by violence have both been rising rather than falling. The coming months and years do not look much better. Just think of the disruptions that would result if Trump wins a second term, or if the situation in the Western Balkans escalates, or if Putin tries to do to Georgia and Moldova what he is doing to Ukraine. There are dozens of other hotspots at risk of boiling over, partly as a consequence of the climate crisis. While the idea of returning

to normalcy might personally appeal to many Germans after the disruption of the pandemic, it surely does not reflect reality around the world – and not even in Europe.

At the same time, in real terms, what Germany can buy for its foreign and development euros has already been brought down to 2017–2019 levels. This is due to last year’s budget cuts coupled with recent macroeconomic trends. While the euro has slightly gained in comparison to many other currencies, rampant inflation – particularly high in developing countries and countries experiencing violent conflict – has more than eaten up those gains. This puts German diplomats, development experts and defense planners a step back in terms of their purchasing power.

While the limited published data makes it difficult to calculate the precise trend in real budgets, it is possible to estimate its range. In practice, both the Foreign Office and the BMZ spend part of their money in Germany – on headquarters staff, building maintenance and so on – and another, larger part abroad. So, calculating real budgets based on Germany’s official inflation figures yields a maximum estimate, while a minimum estimate can be derived by adjusting the same budgets by the IMF’s official global inflation figures (and controlling for the euro’s gains against a basket of international currencies). This is the window for how the real purchasing power of Germany’s foreign affairs and development budgets changed in recent years, illustrated in the shaded area of the chart below.

What Germany is getting for its foreign affairs and development euros, 2017-2025 (in billions of 2015 euros) vs. global displacement trends (in million persons)



This chart shows that not only are real budgets down since 2021, but that they have already dropped below the Finance Ministry’s “pre-crisis” target for 2025. Now, while needs are spiking, Germany is effectively getting less for each nominal euro than seven years ago.

In geopolitical terms, it is becoming more expensive to maintain influence; in humanitarian terms, there are ever more people requiring assistance to survive. Since 2017, the number of forcibly displaced people worldwide has tripled to reach over 13 million, according to UNHCR. Letting them starve is neither what progressive voters expect from a Social-Democrat Chancellor or a Green Foreign Minister, nor will it do anything to stem the tide of waning German influence.

What Does This Mean for the Next Election?

With this budget compromise, the Ampel coalition is likely set to complete its full term. Previous FDP threats to withdraw from the government are off the table. Next fall, then, a new governing coalition is going to inherit plenty of problems. Chief among them, in terms of national security, is this: If the next government also sees the need to rebuild German hard power, how will it pay for it? Voters are not going to choose their candidates based on the number of embassies or euros going to aid. Yet the country will need to find a new fiscal basis for investment in security writ large – primarily, defense spending – for there to be space to correct the course of German soft power.

Most likely, the next chancellor will either be CDU chairman Friedrich Merz (the current leader in the polls) or Olaf Scholz again (who may, in another surprising twist similar to the last election, turn out to look a tiny bit less weak than the rest). Both would need partners. Neither is likely to abandon the necessary project of rebuilding the Bundeswehr, but finding a governing majority with a common vision of how to fund that will be difficult. Fifteen months ahead of the election, the center-right is polling below 40 percent and the center-left even short of 30 percent; if conservatives and social democrats were to form another so-called Grand Coalition, they would come in at just under 50 percent. Should they make it over the line, they could follow several conservative state leaders who have already called for reforming debt rules, and find a grand fiscal compromise.

In so doing, they should also prioritize restoring and solidifying a commitment to non-military sources of influence in order to defend German and European interests. Aid and development tools are neither good nor effective enough as they are right now. They need to be evaluated more carefully and used more strategically, with clear targets and a focus on impact – but the same goes for the broken military procurement system. If the country does not make these investments, and spend the time and money needed to make them better, an aging Germany – with a declining economic output and share of the global population – really does risk being left behind by those who are willing to spend what it takes to assert their interests.

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