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**Overview:** In this issue of showCASE, our experts decode the latest energy efficiency debate in the European Union ahead of the upcoming vote on this topic in the European Parliament. We also take a look at the unfolding situation in post-election Germany and discuss possible coalition negotiations scenarios.

## EU and the Future of the Energy Efficiency

By: Marian Mraz, Senior Economist at CASE

An important vote is imminent in the European Parliament on 28 November, a vote whose result will largely determine the Parliament's position in negotiating upcoming amendments of the Energy Efficiency Directive (EED). The European Commission (EC) proposed a revised objective of a 30% binding European Union (EU) energy efficiency target, aiming to align EU energy legislation with its 2030 energy and climate policy goals. The ambition of the European Commission, however, falls far short of the European Parliament 's expectations.

For the European Commission, energy efficiency became one of the five pillars of the 2015 Energy Union strategy with "energy efficiency first" as its key element (simply put, higher energy efficiency means producing the same output using less energy). The framework established by the Energy Efficiency Directive requires Member States to set indicative national energy efficiency targets, ensuring that the EU reaches its overall headline target of saving 20% of primary and final energy consumption by 2020 compared to baseline projections. Moreover, it includes a set of binding measures such as a number of product and building performance standards.


*Photo: Pixabay*

Growing concerns regarding the scale of local air pollution or projected effects of climate change have played an important roles behind the rising interest in energy efficiency from policymakers; however, recently, pursuing energy efficiency has become a priority not only for governments, but also for firms and households. Households can reach substantial savings focusing on their building insulation, lighting and heating practices, or use of electric appliances. In energy-intensive industries, such as iron, steel or cement production, new technologies and better manufacturing processes can decrease the use of energy. Reduced energy use can in turn contribute to better air quality with reduced health impacts, as well as more sustainable use of natural resources. Incentives for improvements in energy efficiency are being translated into the rising demand for new technologies spurring innovation and creating new jobs including for the highly qualified labor force. A study conducted by Cambridge Econometrics confirmed that, according to their estimates, in 2010 alone, the supply of energy-efficient goods and services generated around 900,000 jobs across the EU28.

On the other hand, the environmental implications of rising energy efficiency have a degree of uncertainty depending on actual consumer behavior. Efficiency savings might eventually lead to an increase in energy consumed, causing the so-called 'rebound effect'. For example, insulating a house can make it for cheaper for its residents to maintain a higher temperature. This would increase the residential comfort but reduce energy savings and reductions of CO2 emissions. Research based on EU data suggested that eleven EU Member States have experienced rebound effects of over 50%, with six additional Member States seeing effects of over 100%.

Increasing energy efficiency is also linked with high up-front costs and several other market barriers, a reality that is used as justification for regulatory intervention to transfer the needed finances. However, despite the binding legal instruments on EU firms, it appears that even they are insufficient to meet the ambitious 2020 energy efficiency target. The implementation of the EED has garnered criticism, with the European Parliament noting that current energy efficiency legislation obliges the EU Member States to save an equivalent of 1.5% of energy sold to consumers every year. But due to several gaps in the legislation, the savings achieved across the EU could be reduced to just 0.75%.

The views on the way forward differ. A number of proposals have been shared for circulation prior to the upcoming vote of the members of the industry committee (ITRE) of the European Parliament. They all differ in terms of overall ambition (27%, 30% or 40% reduction of the demand for energy) and degree of binding force (while several EU Member States require indicative targets, the European Commission and the Parliament have pushed for binding reduction commitments at the national level). Remaining differences in the proposals on the table include the way several loopholes in the original Directive should be addressed. The vote of the members of industry committee (ITRE) of the European Parliament will be crucial for further dialogue on the new shape of the framework for energy efficiency policy.

By: Katarzyna Mirecka, Economist at CASE

Photo: Reuters

It has been more than two months since German Chancellor Angela Merkel began her struggle to form a coalition government in the wake of an election where her CDU (Christian Democratic Union of Germany) and its sister CSU (Christian Social Union in Bavaria) received 32% of the votes. Negotiations between the CDU-CSU, Green Party, and the FDP (Free Democratic Party), which were supposed to end in the so-called "Jamaica" coalition, collapsed on the night of November 19th/20th. The FDP, sensing that they were to be the losers in such a coalition, pulled out, with FDP leader Christian Lindner bluntly stating that he believed it was better "not to rule than to rule badly."

The reason for the proposed coalition not meeting its fourth self-imposed deadline was, according to Lindner, lack of "common vision for modernisation of the country or common basis of trust," with the main bone of contention being migration and climate policy. After Ms. Merkel's decision to open German borders to 1.2 million migrants and refugees in 2015-2016, there still remains the question of how many should be allowed to be joined by their families. Perhaps more importantly, Ms. Merkel's highly controversial decision has opened the door for debate on how many migrants and refugees Germany should – and is capable of – welcoming each year. While the Greens opted for an open-door policy, while the other prospective coalition members voted for a strict number of 200,000 immigrants per year.

In respect to climate-related issues, as well, the Green party tried to pull the coalition to the left, calling for a reduction in coal-generated power, which in turn raised concerns from other partners in terms of job losses in the industry. Even though, reportedly, the Greens were ready to find a compromise and accept the limits on migration in return for more environmental regulations, it was not enough for business-friendly FDP to stay in the game, in particular given the remaining 120 points on the coalition partnership agreement yet to resolve.

While various coalition scenarios have been discussed since Merkel's CDU/CSU won the election last September, the Jamaican option seemed (at least recently) the most viable one. With the FDP out of the game, three other options are theoretically possible: minority government, new elections, or coalition with the SPD (Social Democratic Party). The first one scenario is not very likely, since Ms. Merkel herself declared she would rather call a new election than form a minority government. According to polls, the former solution is supported by roughly half (49.9%) of Germans, although another survey showed that should that happen, the result would be very similar to the current one. Some experts fear that after the fiasco of negotiations, new elections could bring even more votes to the xenophobic Alternative for Germany (AfD), who ended up winning 12.6% of votes in September and entered real politics for the first time since its establishment.

Coalition with SPD, in turn, until quite recently seemed possible only in theory: another so-called "grand coalition" had been rejected by SPD's leader, Martin Schulz. After 4 years in coalition with the CDU/CSU and the worst election result in the post-war history, he announced his party would move to the opposition. However, last Friday, after a meeting with the German president, Frank-Walter Steinmeier, the situation reversed. This quite uncommon move (German presidents are traditionally mostly ceremonial) led to Mr. Schulz declaring that his party is ready to negotiate with CDU/CSU. Around the same time, the Conservatives voted in favour of this solution as well. Whether a new "grand coalition" will be re-established, or will SPD provide informal political support to a minority CDU/CSU and Green Party government, remains uncertain at the moment.

Even though the SPD's U-turn decision certainly is a good sign, Ms. Merkel and her colleagues are not raising champagne (or beer) glasses quite yet. For one, not everyone in both parties is in favor of the new coalition. Moreover, seeing Merkel in despair, the SPD may enter negotiations with exaggerated demands, which may in turn lead to another negotiations fiasco. Migration quotas could also possibly become a major point of contention again: while the SPD claims any kind of limits are unacceptable, Ms. Merkel needs to impose a cap of 200,000 in order to maintain a good relationship with the conservative CSU. Finally, even if they do manage to reach an agreement, a grand coalition would have a side effect of the far-right AfD becoming the biggest opposition party in Bundestag. Whatever the outcome of negotiations, then, it will be more and more difficult for the Chancellor to claim that the current political situation in the country is nothing but yet another challenge to overcome.

While long coalition negotiations are by no means unusual in the world of politics, for Germany the present situation represents the worst political crisis since the end of the war. Usually described using the word "stable," Germany has had Ms. Merkel in the office for the last 12 years and she can conceivably stay for 4 years more. Political confusion, or even instability, in the biggest economy in the European Union is therefore something new. The first of the many possible consequences has already been observed in the decrease of the value of the Euro. Moreover, Merkel's weakened position might be an obstacle to deeper economic integration in the EU and in solving key issues in Brussels. Taking a broader look at the current situation the EU faces, with Russia's invasion in Ukraine and war in Syria, a fragile relationship with Turkey, an on-going migration crisis, and the spectre of populist movements across Europe, German political stagnation is coming at the most inopportune time.

**This week:** More than 338,000 Polish citizens have applied for early retirement since the law lowering the retirement age came into force in October this year. It is estimated that, by the end of the year, a full 410,000 people may retire – 80,000 more than the government initially predicted. As this will generate an additional burden for the state budget, the government is expected to introduce measures aimed at counteracting their own previous policy.

**GDP (Q3 2017)**

**5.0% y/y (est.)**

Up from 4.2% in Q2

**Inflation (Oct 2017)**

**2.1% y/y**

Down from 2.2% in Sep

**Unemployment (Sep 2017)**

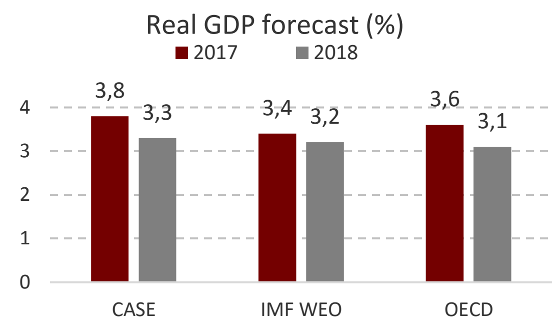
**6.6%**

Down from 6.8% in Aug

**NBP Base rate**

**1.5%**

From 2% Mar 2015




**This week:** Russian economy minister, Maxim Oreshkin, made an official announcement last week concerning the OPEC oil deal, saying that curbing oil output has negatively influenced Russian economy in October. This declaration puts into question the official Russian position to be presented at next week's OPEC meeting in Vienna, where the cartel's members are supposed to discuss its possible extension until late 2018.

**GDP (Q3 2017)**

**1.8% y/y (est.)**

Down from 2.5% in Q2

**Inflation (Oct 2017)**

**2.7% y/y**

Down from 3.0% in Sep

**Unemployment (Oct 2017)**

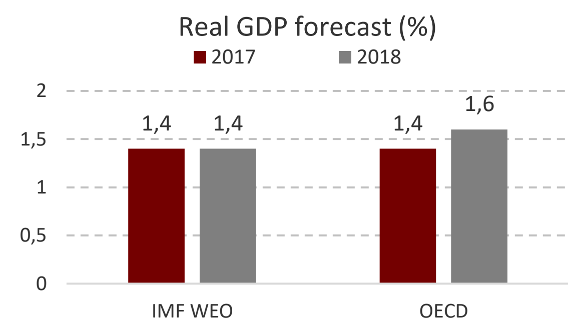
**5.1%**

Up from 5.0% in Sep 2017

**CBR Base rate**

**8.25 %**

From 8.5% in Oct 2017




**This week:** Despite political uncertainty, the construction industry continues to benefit from the boom in real estate and low interest rates. The number of contracts signed increased by 2.9% y-o-y up to 6 billion EUR, reaching an 18-year high. It is expected the industry turnout will increase even further this year.

**GDP (Q3 2017)**

**2.8% y/y**

Up from 2.3% in Q2

**Inflation (Oct 2017)**

**1.5% y/y**

From 1.8% in Sep

**Unemployment (Sep 2017)**

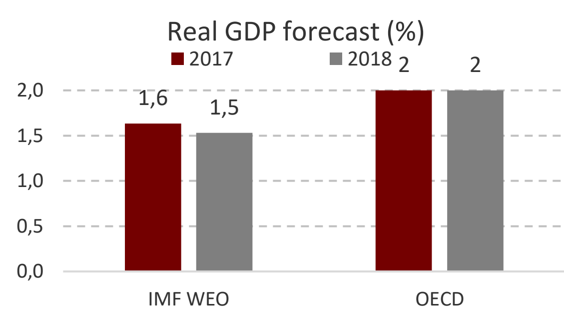
**3.5%**

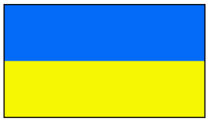
Up from 3.7% in August

**ECB Deposit rate**

**-0.4%**

From -0.3% Dec 2015





**This week:** Alexei Doroshenko, Chairman of the Ukrainian Association of Trade Network Suppliers, declared that since the beginning of the year the "Ukrainian borscht index" increased by 33% or by 20 hryvnia, from 61 hryvnia up to 81 hryvnia. The index is used to showcase inflation and is modeled on the famous "Big Mac index."

**GDP (Q3 2017)**

**2.1% y/y**

From 2.5% in Q1

**Inflation (Oct 2017)**

**14.6% y/y**

Up from 16.2% in Aug

**Unemployment (Q2 2017)**

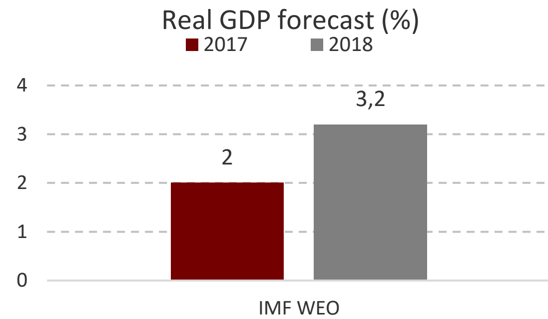
**9.1%**

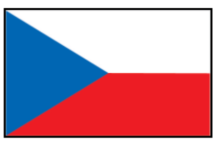
Down from 10.5% in Q1 2017

**NBU Base rate**

**13.5%**

From 12.5% in Sep 2017



**This week:** The largest delegation of Czech entrepreneurs in history, led by the president Miloš Zeman, visited the Russian Federation. During the trip, nine new contracts and agreements worth roughly 19 billion Czech korunas were signed. The biggest deal was completed between Zetor Tractors and Russia's KEMZ, with an estimated worth over the next four years of 14 billion korunas.

**GDP (Q3 2017)**

**5.0% y/y**

Up from 4.7% in Q2 2017

**Inflation (Oct 2017)**

**2.9% y/y**

Up from 2.7% in September

**Unemployment (Q3 2017)**

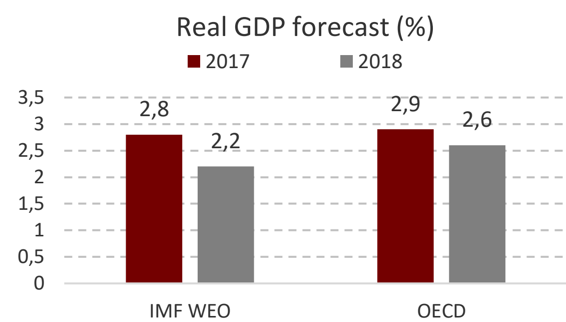
**2.8% (est.)**

Down from 3.0% in Q2

**CNB Base rate**

**0.50%**

From 0.25% (3rd November 2017)




**This Week:** On November 10th, Fitch Ratings upgraded Hungary's long-term foreign- and local-currency outlook from 'stable' to 'positive' and confirmed a Long-Term Issuer Default Rating at of 'BBB-'. The improvement was attributed to "a combination of high current account surpluses, European Union inflows, and private and public sector external deleveraging."

**GDP (Q3 2017)**

**3.6% y/y (est.)**

Down from 4.2% in Q1

**Inflation (Oct 2017)**

**2.2% y/y**

Up from 2.1% in July

**Unemployment (Q2 2017)**

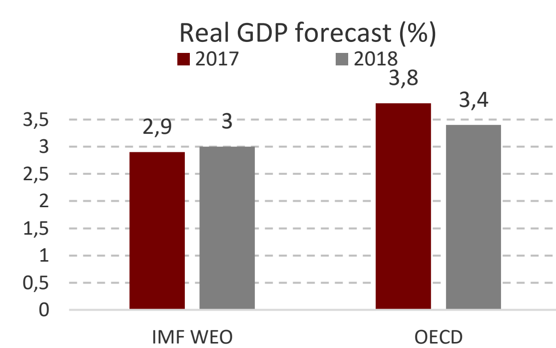
**4.2%**

Down from 4.3% in Q1

**MNB Base rate**

**0.9%**

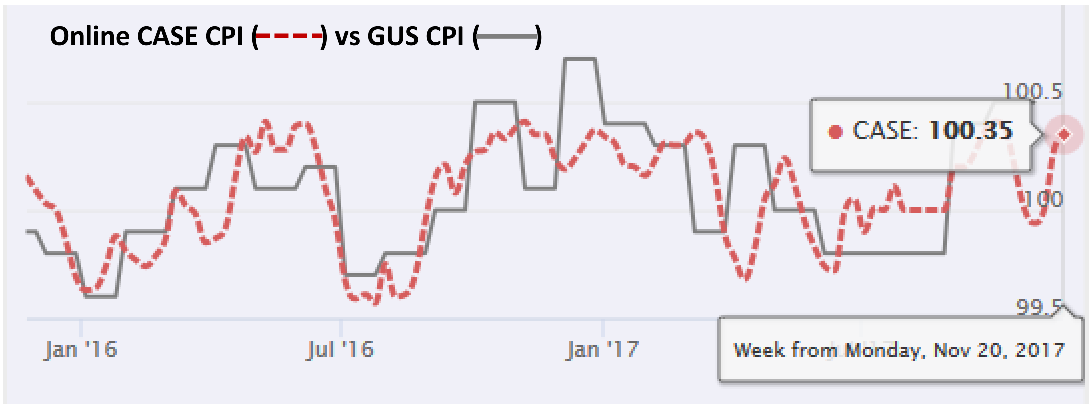
From 1.05% May 2016



**The weekly online CASE CPI**

The online CASE CPI is an innovative measurement of price dynamics in the Polish economy, which is entirely based on online data. The index is constructed by averaging prices of commodities from the last four weeks and comparing them to average prices of the same commodities from four weeks prior. The index is updated weekly.

**Our weekly online CASE CPI**




**Monthly CASE forecasts for the Polish economy**

Every month, CASE experts estimate a range of variables for the Polish economy, including future growth, private consumption, and foreign trade, current account balance, and the CPI.

**CASE economic forecasts for the Polish economy**
***(average % change on previous calendar year, unless otherwise indicated)***

| | GDP | Private consumption | Gross fixed investment | Industrial production | Consumer prices |
|---|---|---|---|---|---|
| **2017** | 3.8 | 4.3 | 2.7 | 4.3 | 1.9 |
| **2018** | 3.3 | 3.3 | 3.1 | 3.7 | 2.1 |
| | **Nominal monthly wages** | **Merchandise exports (USD, bn)** | **Merchandise imports (USD, bn)** | **Merchandise trade balance (USD, bn)** | **CA balance (USD, bn)** |
| **2017** | 5.1 | 201.6 | 201.8 | -0.2 | -4.7 |
| **2018** | 3.5 | 211.3 | 213.1 | -1.8 | -5.9 |

For more information on our weekly online CASE CPI, please visit: http://case-research.eu/en/online-case-cpi
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