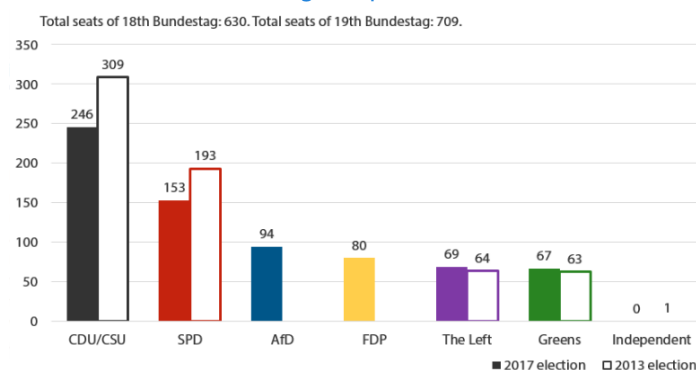


# GERMANY'S ELECTION RESULTS – WHAT NOW?

Unsurprisingly, Angela Merkel will continue as German chancellor for a fourth term. But the rest of the election results were perhaps less expected. Germany went to the polls on 24 September, and Merkel's centre-right Christian Democratic Union/Christian Social Union (CDU/CSU) party emerged as the largest party in parliament, albeit with a smaller share of the vote than had been suggested by recent polls and at a post-war low. Its partner in the 'Grand Coalition', the Social Democrats (SPD), also saw its worst post-war result with 20.7% of the vote. The SPD subsequently announced it would not join another coalition, instead opting to form the main opposition party.

The big winners included the far-right populist Alternative for Germany (AfD), which garnered 13% of the vote, granting it entry into parliament for the first time, and as the third-largest party. The business-friendly Free Democratic Party (FDP) and the Green Party also improved their standings from the previous election, with about 10.5% and 9% of the vote respectively.

Chart 1: German Bundestag composition – number of seats



Source: Bundeswahlleiter, Mizuho International

## The challenging road ahead

Now, Chancellor Merkel faces weeks, if not months, of difficult coalition negotiations. She will likely end up forming the 'Jamaica' coalition, named for the party colours of the CDU (black), FDP (yellow) and the Greens. That said, these parties have conflicting positions on issues ranging from Eurozone integration, to immigration, to the economy and the environment.

**Well-aware that Merkel's previous junior coalition partners ended up with hefty defeats in the following elections, the Greens and the FDP will be looking to ensure there is enough in the coalition deal to differentiate themselves from Merkel and her politics.** We expect both parties to focus on their agendas in specific areas (education and digitalisation for the FDP, and the phase-out of petrol and diesel engines by 2030 for the Greens), while leaving other fields to the CDU. In this way, they will hopefully in four years be able to show some meaningful results to their voters.

Nevertheless, negotiations will be complex, and both the FDP and Greens will enter the talks with substantial pre-conditions. For instance, the FDP deeply opposes French President Emmanuel Macron's campaign proposal for a more integrated Eurozone, with a shared budget and its own finance minister. Any agreement that France and Germany eventually reach regarding the Eurozone may not have the scope that Macron had hoped for.

On top of this, Merkel will also have to deal with the conservatives within her own party. She has been criticised for positioning the party in the political centre, which has lost them voters to the AfD. It remains to be seen if she will manoeuvre more to the right to win some AfD voters back. Her future policies on migration and refugees will therefore be closely watched.

The CDU will also have to resolve differences with its Bavarian sister party, the CSU. The AfD's surge of popularity in Bavaria has sparked concern that the CSU may lose its majority in the Bavarian state elections in 2018. The CSU could therefore be tempted to take a harder line on immigration policy. It has indicated that it will be negotiating for a hard cap on the number of refugees entering Germany, a position that Merkel, as well as the FDP and Greens, have rejected.

## We expect Jamaica talks to ultimately succeed

Coalition building talks are not expected to begin until mid-October, after state elections in Lower Saxony, one of Germany's largest states. Merkel is hoping to have a new government in place by Christmas.

In the event that coalition talks fail, however, there is a risk that new elections are called and Germans would have to go through the process of voting for their parliament again. However we think this is very unlikely to happen. None of the parties involved would want to be seen as responsible for

bringing the country to a standstill by triggering snap elections.

Ultimately, despite the differences in ideology, all the involved parties know it is their responsibility to come up with a solution and form a government. Germany, in its democratic history since 1949, has always been ruled by coalition and politicians are used to reaching consensus. Merkel, too, has significant experience in bridging differences and working towards agreement. While it might take a little longer this time, **we believe that the CDU, FDP and Greens will eventually form a stable government.**

## Conclusion

Despite the uncertainty surrounding the time it will take before the formation of a new government, we do not think there is risk of major policy change in Germany. [As we stated in our pre-election commentary](#), it is unlikely that any government coalition will implement significant structural reforms.

The election outcome, however, will likely weigh on the aspirations of France's Macron for deeper Eurozone integration. Germany's finance minister Wolfgang Schäuble, who was largely seen as pro-European, is stepping down to become speaker of the Bundestag. The finance ministry could now go to the FDP, which, as previously mentioned, would likely be less amenable to Macron's proposals.

We continue to see attractive opportunities within German corporate bonds. Our preference for the health care and auto parts sectors remains unchanged, as they remain beneficiaries of the strong economy and continue to provide appealing yields.

## Important Information

This document is prepared by Nikko Asset Management Co., Ltd. and/or its affiliates (**Nikko AM**) and is for distribution only under such circumstances as may be permitted by applicable laws. This document does not constitute investment advice or a personal recommendation and it does not consider in any way the suitability or appropriateness of the subject matter for the individual circumstances of any recipient.

This document is for information purposes only and is not intended to be an offer, or a solicitation of an offer, to buy or sell any investments or participate in any trading strategy. Moreover, the information in this material will not affect Nikko AM's investment strategy in any way. The information and opinions in this document have been derived from or reached from sources believed in good faith to be reliable but have not been independently verified. Nikko AM makes no guarantee, representation or warranty, express or implied, and accepts no responsibility or liability for the accuracy or completeness of this document. No reliance should be placed on any assumptions, forecasts, projections, estimates or prospects contained within this document. This document should not be regarded by recipients as a substitute for the exercise of their own judgment. Opinions stated in this document may change without notice.

In any investment, past performance is neither an indication nor guarantee of future performance and a loss of capital may occur. Estimates of future performance are based on assumptions that may not be realised. Investors should be able to withstand the loss of any

principal investment. The mention of individual stocks, sectors, regions or countries within this document does not imply a recommendation to buy or sell.

Nikko AM accepts no liability whatsoever for any loss or damage of any kind arising out of the use of all or any part of this document, provided that nothing herein excludes or restricts any liability of Nikko AM under applicable regulatory rules or requirements.

All information contained in this document is solely for the attention and use of the intended recipients. Any use beyond that intended by Nikko AM is strictly prohibited.

**Japan:** The information contained in this document pertaining specifically to the investment products is not directed at persons in Japan nor is it intended for distribution to persons in Japan. Registration Number: Director of the Kanto Local Finance Bureau (Financial Instruments firms) No. 368 Member Associations: The Investment Trusts Association, Japan/Japan Investment Advisers Association/Japan Securities Dealers Association.

**United Kingdom and rest of Europe:** This document constitutes a financial promotion for the purposes of the Financial Services and Markets Act 2000 (as amended) (FSMA) and the rules of the Financial Conduct Authority (the FCA) in the United Kingdom (the FCA Rules).

This document is communicated by Nikko Asset Management Europe Ltd, which is authorised and regulated in the United Kingdom by the FCA (122084). It is directed only at (a) investment professionals falling within article 19 of the Financial Services and Markets Act 2000 (Financial Promotions) Order 2005, (as amended) (the Order) (b) certain high net worth entities within the meaning of article 49 of the Order and (c) persons to whom this document may otherwise lawfully be communicated (all such persons being referred to as relevant persons) and is only available to such persons and any investment activity to which it relates will only be engaged in with such persons.

**United States:** This document is for information purposes only and is not intended to be an offer, or a solicitation of an offer, to buy or sell any investments. This document should not be regarded as investment advice. This document may not be duplicated, quoted, discussed or otherwise shared without prior consent. Any offering or distribution of a Fund in the United States may only be conducted via a licensed and registered broker-dealer or a duly qualified entity. Nikko Asset Management Americas, Inc. is a United States Registered Investment Adviser.

**Singapore:** This document is for information only with no consideration given to the specific investment objective, financial situation and particular needs of any specific person. You should seek advice from a financial adviser before making any investment. In the event that you choose not to do so, you should consider whether the investment selected is suitable for you. Nikko Asset Management Asia Limited is a regulated entity in Singapore.

**Hong Kong:** This document is for information only with no consideration given to the specific investment objective, financial situation and particular needs of any specific person. You should seek advice from a financial adviser before making any investment. In the event that you choose not to do so, you should consider whether the investment selected is suitable for you. The contents of this document have not been reviewed by the Securities and Futures Commission or any regulatory authority in Hong Kong. Nikko Asset Management Hong Kong Limited is a licensed corporation in Hong Kong.

**Australia:** Nikko AM Limited ABN 99 003 376 252 (**Nikko AM Australia**) is responsible for the distribution of this information in Australia. **Nikko AM Australia** holds Australian Financial Services Licence No. 237563 and is part of the Nikko AM Group. This material and any offer to provide financial services are for information purposes only. This material does not take into account the objectives,

financial situation or needs of any individual and is not intended to constitute personal advice, nor can it be relied upon as such. This material is intended for, and can only be provided and made available to, persons who are regarded as Wholesale Clients for the purposes of section 761G of the Corporations Act 2001 (Cth) and must not be made available or passed on to persons who are regarded as Retail Clients for the purposes of this Act. If you are in any doubt about any of the contents, you should obtain independent professional advice.

**New Zealand:** Nikko Asset Management New Zealand Limited (Company No. 606057, FSP22562) is the licensed Investment Manager of Nikko AM NZ Investment Scheme and the Nikko AM NZ Wholesale Investment Scheme.

This material is for the use of researchers, financial advisers and wholesale investors (in accordance with Schedule 1, Clause 3 of the Financial Markets Conduct Act 2013 in New Zealand). This material has been prepared without taking into account a potential investor's objectives, financial situation or needs and is not intended to constitute personal financial advice, and must not be relied on as such. Recipients of this material, who are not wholesale investors, or the named client, or their duly appointed agent, should consult an Authorised Financial Adviser and the relevant Product Disclosure Statement or Fund Fact Sheet (available on our website [www.nikkoam.co.nz](http://www.nikkoam.co.nz)).

**Kingdom of Bahrain:** The document has not been approved by the Central Bank of Bahrain which takes no responsibility for its contents. No offer to the public to purchase the Strategy will be made in the Kingdom of Bahrain and this document is intended to be read by the addressee only and must not be passed to, issued to, or shown to the public generally.

**Kuwait:** This document is not for general circulation to the public in Kuwait. The Strategy has not been licensed for offering in Kuwait by the Kuwaiti Capital Markets Authority or any other relevant Kuwaiti government agency. The offering of the Strategy in Kuwait on the basis a private placement or public offering is, therefore, restricted in accordance with Decree Law No. 7 of 2010 and the bylaws thereto (as amended). No private or public offering of the Strategy is being made in Kuwait, and no agreement relating to the sale of the Strategy will be concluded in Kuwait. No marketing or solicitation or inducement activities are being used to offer or market the Strategy in Kuwait.

**Kingdom of Saudi Arabia:** This document is communicated by Nikko Asset Management Europe Ltd (Nikko AME), which is authorised and regulated by the Financial Services and Markets Act 2000 (as amended) (FSMA) and the rules of the Financial Conduct Authority (the FCA) in the United Kingdom (the FCA Rules). This document should not be reproduced, redistributed, or sent directly or indirectly to any other party or published in full or in part for any purpose whatsoever without a prior written permission from Nikko AME.

This document does not constitute investment advice or a personal recommendation and does not consider in any way the suitability or appropriateness of the subject matter for the individual circumstances of any recipient. In providing a person with this document, Nikko AME is not treating that person as a client for the purposes of the FCA Rules other than those relating to financial promotion and that person will not therefore benefit from any protections that would be available to such clients.

Nikko AME and its associates and/or its or their officers, directors or employees may have or have had positions or material interests, may at any time make purchases and/or sales as principal or agent, may provide or have provided corporate finance services to issuers or may provide or have provided significant advice or investment services in any investments referred to in this document or in related investments. Relevant confidential information, if any, known within any company in the Nikko AM group or Sumitomo Mitsui Trust Bank group and not available to Nikko AME because of regulations or

internal procedure is not reflected in this document. The investments mentioned in this document may not be eligible for sale in some states or countries, and they may not be suitable for all types of investors.

**Oman:** The information contained in this document neither constitutes a public offer of securities in the Sultanate of Oman as contemplated by the Commercial companies law of Oman (Royal decree 4/74) or the Capital Markets Law of Oman (Royal Decree 80/98), nor does it constitute an offer to sell, or the solicitation of any offer to buy non-Omani securities in the Sultanate of Oman as contemplated by Article 139 of the Executive Regulations to the Capital Market law (issued by Decision No. 1/2009). This document is not intended to lead to the conclusion of any contract of whatsoever nature within the territory of the Sultanate of Oman.

**Qatar (excluding QFC):** The Strategies are only being offered to a limited number of investors who are willing and able to conduct an independent investigation of the risks involved in an investment in such Strategies. The document does not constitute an offer to the public and should not be reproduced, redistributed, or sent directly or indirectly to any other party or published in full or in part for any purpose whatsoever without a prior written permission from Nikko Asset Management Europe Ltd (Nikko AME). No transaction will be concluded in your jurisdiction and any inquiries regarding the Strategies should be made to Nikko AME.

**United Arab Emirates (excluding DIFC):** This document and the information contained herein, do not constitute, and is not intended to constitute, a public offer of securities in the United Arab Emirates and accordingly should not be construed as such. The Strategy is only being offered to a limited number of investors in the UAE who are (a) willing and able to conduct an independent investigation of the risks involved in an investment in such Strategy, and (b) upon their specific request.

The Strategy has not been approved by or licensed or registered with the UAE Central Bank, the Securities and Commodities Authority or any other relevant licensing authorities or governmental agencies in the UAE. This document is for the use of the named addressee only and should not be given or shown to any other person (other than employees, agents or consultants in connection with the addressee's consideration thereof).

No transaction will be concluded in the UAE and any inquiries regarding the Strategy should be made to Nikko Asset Management Europe Ltd.