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To the point!

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Germany's fuel price brake is a dead end

Berlin's response to high fuel prices is costly and poorly targeted

On Monday, Berlin breathed a sigh of relief. After a marathon meeting of Germany's governing coalition leaders over the weekend in the grand Villa Borsig – a government guest house on Lake Tegel in the north of the capital – they finally hammered out a compromise. In the days before, the federal finance minister and the economics minister had been publicly at loggerheads over whether and how to ease the burden on motorists.

Now the coalition plans to waive part of the energy tax on petrol and diesel for two months. That could cut fuel prices by up to 17 cents per liter. On top of that, companies will be allowed to pay their employees a tax-free relief bonus of up to EUR 1,000. According to estimates by the German Economic Institute (IW), this measure alone could reduce revenues from taxes and social contributions by as much as EUR 12 bn. It is highly doubtful that the planned increase in tobacco tax, intended as an offsetting measure, can make up for that. Tobacco tax receipts totaled less than EUR 16 bn in 2024. But apparently money is no object.

Criticism was not long in coming. Monika Schnitzer, chair of Germany's Council of Economic Experts – an independent advisory body to the government – argued that a temporary cut in energy tax for everyone was the worst option on the table. She is pointing in the right direction.

Missing the point

The core problem with the “solution” now agreed is that it meddles with market mechanisms while ignoring the actual trigger. Because of the war in Iran and the blockade of the Strait of Hormuz, the world is facing a shortage of oil products. A problem that originated in the Gulf region cannot be solved on the shores

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End of the
wrangling
in Berlin

The government
cannot fix the
underlying
problem

of Lake Tegel by administrative decree. Prices are sending a scarcity signal.

If the German government now undermines the market mechanism, it removes the incentive to change behavior – to drive less, or more efficiently. If industrialized countries slow the necessary reduction in demand at home, that inevitably means energy scarcity will increase elsewhere in the world. The policy therefore affects people living in poorer countries whose governments lack the means to subsidize the problem away. But that, it seems, is deemed too far away to matter.

Blunt instruments

Even domestically, the distributional impact is questionable. The measures do not, after all, specifically target low-income households. Instead, those who drive long distances with powerful petrol and diesel cars benefit disproportionately. Many in this group are likely perfectly able to afford higher prices. Once again – as during the pandemic – the government is taking a scattergun approach, sprinkling money widely rather than aiming carefully. And that is assuming, optimistically, that the oil industry will pass on the tax cut in full to consumers at the pump. Past experience with reduced VAT for restaurants in Germany counsels skepticism. On top of that, because of the legislative process in parliament, the relief will not take effect before May at the earliest.

It would have been better to introduce a flat-rate energy bonus for everyone, or targeted schemes for haulage companies, tradespeople, taxi operators, social services and the like – sectors where high petrol prices really bite. Alternatively, the government could have cut electricity tax – which would benefit all citizens, not just those who drive combustion-engine vehicles.

Politically, the decision is understandable

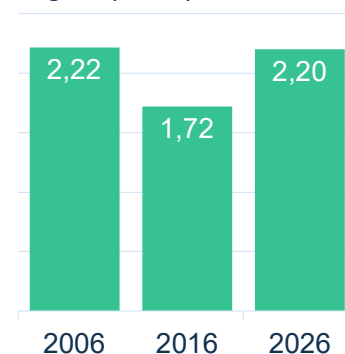
Seen through a political lens, it becomes clear why economists' pro-market positions have little appeal. Populists – especially on the right – are driving the coalition ahead of them on this issue. The far-right Alternative for Germany (AfD) party, unsurprisingly, wasted no time in pouring scorn on the decision: too little, too late. It is easy to heckle from the opposition benches.

All the same, it is regrettable that any economic hardship now reflexively triggers calls for state support. One key fact tends to be forgotten: we all end up picking up the tab via higher public debt. In the end, the state is all of us.

Finally, if you compare fuel prices with the trend in nominal wages, the average employee today does not have to work longer to pay for a liter of premium petrol than twenty years ago (see chart 1). The supposed “price explosion” exists only in nominal terms. In reality, it is little more than an optical illusion.

Dubious distributional effects

Fig. 1: Germany: average price for one liter petrol, adjusted for nominal wages (EUR)



Source: [Benzinpreis.de](https://www.benzinpreis.de), [Destatis](https://www.destatis.de), LBBW Research

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