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## **New reform plans, old medicine**

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### Abstract

The reform plans are intended to give the economy a new lease of life. However, if the approach relies primarily on subsidies, the hoped-for effect is unlikely to materialize.

### Zusammenfassung

Die Reformpläne sollen der Wirtschaft neuen Schwung geben. Doch wenn der Therapieansatz vor allem auf Subventionen setzt, dürfte die erhoffte Wirkung ausbleiben.



If a doctor prescribes a medicine but the treatment fails to work, it stands to reason that the medicine is not effective. A different therapeutic approach is needed. This logic is taken for granted in medicine. In politics, however, it receives far less attention.

The reform package presented last Thursday by the coalition leaders is intended to aid the economy's recovery. The coalition is relying on different therapies for different economic conditions. The [reform plan put forward by the CDU/CSU and SPD](#) provides for the consistent promotion of so-called 'industries of the future'. These include, amongst others, the automotive sector, the chemical and pharmaceutical industries, semiconductor production and the field of artificial intelligence. These sectors, declared to be 'technologies of the future', are intended to serve as the pillars of the German economy in future.

### **But what does 'support' mean in this context?**

Generally speaking, 'promotion' is understood to mean financial support for businesses. This can take the form of direct support, such as investment aid or operating cost subsidies, or indirect measures such as tax breaks, low-interest loans and financial relief for consumers. Support of this kind can be grouped under the umbrella term 'subsidies'.

In recent years, subsidies have been a favoured instrument of German economic policy for supporting companies or driving forward an economic transformation in line with political objectives. The idea of using state funds to achieve political goals is tempting – particularly as China appears to be succeeding with its industrial policy. In Germany, however, success has so far eluded us.

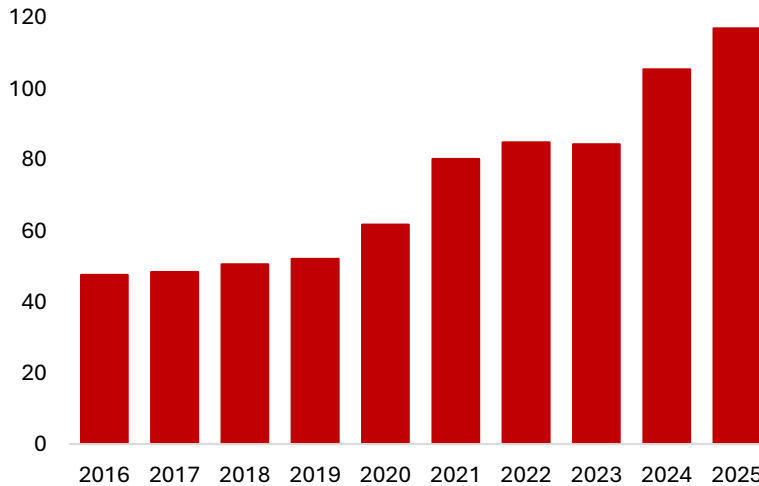
### **Subsidies are a popular remedy**

According to [figures from the Federal Government](#), over the past 10 years the federal government, the federal states and local authorities have provided the German economy with subsidies totaling 780 billion euros. The annual volume of subsidies rose from just under 50 billion euros in 2016 to almost 120 billion euros in 2025 (Fig. 1). For the current year, the targeted subsidy amount remains at the same level.



### Fig. 1: Subsidies in Germany

according to figures from the Federal Government, in billions of euros



Source: Federal Government subsidy reports, Federal Ministry of Finance.  
As at July 2026.

The German automotive industry, in particular, has benefited. The major German car manufacturers alone – Volkswagen, BMW, Mercedes-Benz, Porsche, Traton and Daimler Truck – report direct grants totalling 14.7 billion euros for the period from 2013 to 2024.<sup>1</sup> Furthermore, the companies benefited indirectly to the tune of billions from tax relief and subsidies for consumers of their products, such as the environmental bonus and the electric car incentive. Further direct and indirect subsidies worth billions were provided along the vertical value chain. However, the automotive industry has not yet recovered. On the contrary, it is one of the German economy’s most critical cases.

### Why is recovery taking so long, despite the high-dose ‘taxpayer-funded medicine’?

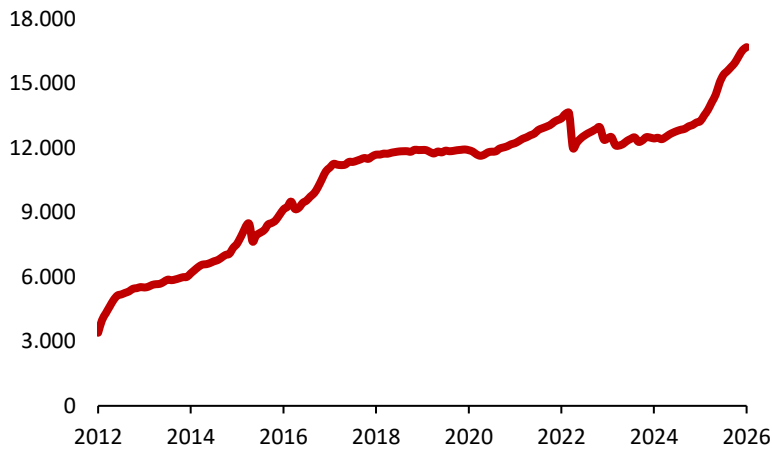
The challenges facing the German economy are complex and vary from company to company. Fundamentally, these financial injections do not resolve the underlying location-specific problems in the form of high energy, labour and bureaucratic costs. Nor can purchasing decisions in the Far East for or against German cars, trade barriers, raw material shortages and supply chain problems generally be resolved through the local allocation of subsidies.

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<sup>1</sup> Figures from the annual reports for the years 2013 to 2024 relating to government grants in accordance with IAS 20. Tax relief and indirect subsidies are not included in these figures. Source: Companies’ annual reports for the years 2013 to 2024. Calculations by the Flossbach von Storch Research Institute.



**Fig. 2: Number of lobbying organisations in Brussels**



Source: EU Transparency Register, as at July 2026

More seriously, however, the subsidies are accompanied by significant side effects. This is because subsidies alter the behaviour of companies – and usually not in a way that serves political objectives. Subsidies provide incentives for companies to become more involved in exerting political influence, rather than investing in innovation and efficiency. The extent of this ‘rent-seeking’ (see [Olsen 1965](#)) is evident from the sharp rise in the number of lobbyists in Brussels and other capital cities. Over 16,000 lobbying organisations are currently listed in the [EU Transparency Register](#) (Fig. 2). Since 2012, this number has quadrupled. [Lobby Control](#) puts the total budget of all lobbyists in Brussels for the past year at 1.5 billion euros.

The state often subsidises investments that companies would have made even without financial support (see [García-Quevedo 2004](#)). These ‘free-riding effects’ are evident in various sectors of industry. For example, research by the Taxpayers’ Association has identified free-riding effects in the retail sector and in aircraft manufacturing ([Warneke 2024](#)). The [environmental bonus scheme](#) also suffered significantly from free-riding effects. According to surveys, a third of buyers would have purchased an electric car even without the subsidy ([Schlomann et al. 2024](#)).

Once a subsidy has been granted, a second phase begins for companies, known as ‘rent defending’ (see [Krueger 1974](#)). As companies have adapted their business models to the subsidy, when the subsidy comes to an end, political pressure builds to extend it, because the business model would be less lucrative – or often even unsustainable – without it. The farmers’ protests against the phasing out of the agricultural diesel subsidy in the winter of 2023/2024 demonstrated this dynamic impressively. In particular, well-organised groups with significant bargaining power prevail, whilst the general public is left to bear the costs.



Subsidies chart a course for development without it being clear whether the subsidised technologies or companies can hold their own in the market in the long term even without state support. There is a risk that capital and labour will be tied up in unsustainable enterprises using taxpayers' money. Admittedly, based on current knowledge, certain sectors can be identified as 'technologies of the future'. However, it is uncertain whether this assessment will prove correct in the long term. According to F.A. Hayek, the overconfidence of government decision-makers constitutes a 'pretence of knowledge' ([Hayek 1977](#)). Neither public authorities nor companies can reliably predict which technology, or which company will prevail in the long term. The example of the battery manufacturer Northvolt illustrates just how costly the presumption of knowledge can be. Despite government funding commitments running into the billions, the company went into insolvency, which is proving costly for German taxpayers (see [Salto et al. 2026](#)).

Subsidies perpetuate inefficient structures. If a company receives financial support despite lagging its competitors, capital and labour are tied up in areas where they are lacking elsewhere, where they could be deployed more productively. If state aid becomes a permanent fixture, there is a risk of the 'zombification' of entire companies or sectors. The consequences are sluggish growth and a loss of welfare, the burden of which is ultimately borne by society.

Similarly, subsidies represent a redistribution of wealth within the population in favour of the recipient groups. The public finances the support for individual sectors through taxes, levies or public debt, without necessarily benefiting from it themselves. This can lead to good salaries and secure jobs becoming established in the beneficiary sectors, whilst other sections of society must foot the bill through their tax burden.

As a result, Germany's subsidy policy of recent years is likely to have hindered rather than promoted the necessary structural change in the German economy (see [Immenkötter 2026](#)). And now there are signs that old mistakes are being repeated.

### **Hope for the right therapy**

The vague wording of the reform proposal keeps alive the hope that 'promoting' does not necessarily have to mean 'subsidising'. In fact, the reform programme also includes another kind of remedy: namely, cutting red tape and deregulation. For example, simpler approval rules and the introduction of pilot regions are intended to advance autonomous driving. This would be a therapeutic approach that actually tackles the problem at its root.

Whether the coalition will consistently pursue this path, however, remains to be seen. In recent months, the current federal government has already resorted to the well-known 'subsidy remedy' on several occasions, with the [industrial electricity price](#) and the [electric car subsidy](#). At the same time, Federal Minister for Economic



Affairs [Katherina Reiche](#) has repeatedly expressed a critical stance towards subsidies [on social media](#). The hope remains that this time the coalition will not resort to the same ineffective remedy, but will instead opt for a different, hopefully more effective treatment that tackles the root cause of the problem whilst minimising side effects.

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