German Election Watch

The German election and Greece

Chief Investment Office Americas, Wealth Management | 28 August 2017
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- Outlook: The latest polling still suggests a 75% probability of Merkel retaining the chancellery. But the odds of a grand coalition are markedly lower (60%) given several coalition options. The polls suggest a marked shift to the right of the political spectrum by voters since the last election, with the FDP arguing for a Greek exit from the euro. So the German election outcome will likely have an impact on Greece's planned bailout exit next summer.
- Markets: The election's long-term market impact is significant, given its implications for the speed of European integration, the nominations for European institutions and the German stance toward the Eurozone periphery. We expect the forthcoming Greek bailout exit to be structured in a way that should open a window for Greece to tap bond markets for a number of years. But the proposed debt relief is unlikely to make its debt sustainable and downside risks remain high.
- What we're watching: polls, comments from politicians, the fragile EU-Turkey refugee deal, further Greek bond placements and any ECB comments regarding a potential QE inclusion of Greek government bonds.

German Election Watch

- The election and its implications for Europe, 19 July
- Merkel in pole position after regional elections, 14 May
- Introducing the Q&A, 27 March
- The race is on, 30 January
- Schulz to run against Merkel, 25 January

Table of contents

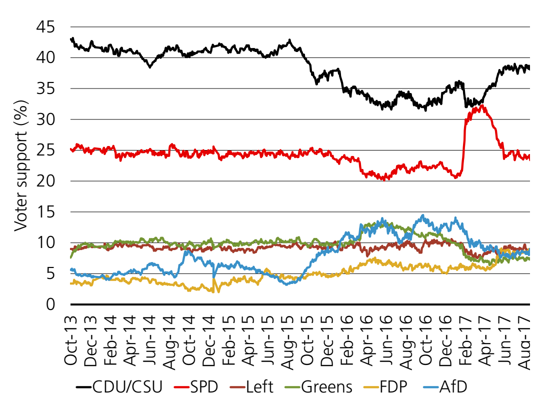
Our view

German polls currently show little volatility as the summer school holidays wind down. We expect little change in them before the TV debate on 3 September between Martin Schulz and Angela Merkel. Merkel appears highly likely to retain the chancellery (CIO estimate: 75%). Her Christian Democratic Union (CDU) and its Bavarian Christian Social Union (CSU) sister party look as if they will have several options for forming a coalition government. The combined voter support of the CDU/CSU with the Free Democratic Party (FDP) or the Greens hovers close to the 50% mark (see Fig. 1).

A coalition with the FDP would probably mean a conservative shift in Germany before the planned Greek bailout exit next summer. Against this backdrop, we examine the implications of the German elections for Greece.

Meanwhile, the successful completion of the second review of the third Greek bailout by official sector creditors has helped lift economic confidence in Greece. Although the country is already on course to deliver its best economic growth rate since the last decade (perhaps exceeding 1% this year), more positive news about the bailout program could lift economic growth past 2% next year. We think that

Fig. 1: Support for political parties
CDU/CSU with a clear lead



Note: Based on the 5-poll moving average of various pollsters. Source: INSA, Emnid, Forsa, Forschungsgruppe Wahlen, GMS, Infratest dimap, Ipsos, Civey, Allensbach, Trend Research, UBS, as of 24 August 2017.

the CDU/CSU's future coalition partner will have an impact on the terms of Greece's bailout exit, but will not halt it (even should it be the FDP). Accordingly, we expect a window opening up for Greece to tap bond markets, even if the proposed debt relief is unlikely to restore debt sustainability, in our view.

German elections and Greece

German election backdrop/polls

We allocate a 75% probability to Merkel retaining the chancellery. Recent polls have not only cemented the CDU/CSU's lead of over 17 percentage points over the Social Democratic Party (SPD), but also the rise of the Greens and the FDP. Although we still see a 60% chance of a grand coalition, political uncertainty has increased markedly. Indeed, potential coalition options other than a grand coalition are now more numerous, bringing possible two-way coalitions with either the FDP or the Greens close to the 50% mark (see Fig. 2).

Germany: A shift toward the right

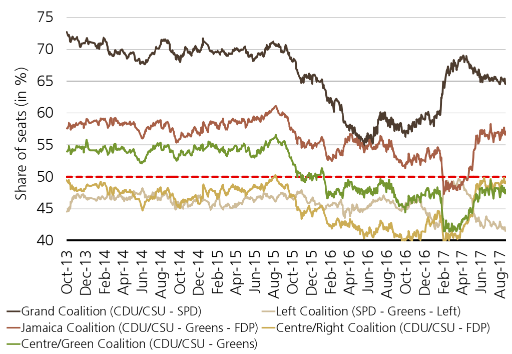
Comparing current polling with the results of previous elections indicates a marked shift to the right. Two parties are polling significantly better than in 2013. The Alternative for Germany (AfD) is set to become the first right-wing party to enter the Bundestag. It is currently polling four percentage points higher than it did in the last Bundestag election. The conservatives from the FDP are also eyeing an increase over 2013 (four percentage points). The CDU, CSU, SPD and the Greens have all lost ground, with the left printing a marginal increase (see Fig. 3).

Tougher German stance in the run-up to the elections

This dynamic may incentivize the government to adopt a tougher stance before the elections. Earlier this year in the Netherlands, Mark Rutte's VVD took a tough line toward Turkey just before the election. This earned his party critical votes at the expense of Geert Wilder's right-wing PVV party. The German relationship with Turkey has recently taken a sharp turn for the worse. As a consequence, risks to the EU-Turkey refugee deal are currently high, in our view. A breakdown in relations could cause a bigger shift to the right (even beyond Germany). In addition, it would mean more pressure on Greece, which currently hosts well over 60,000 refugees. For now, we expect the refugee deal to hold, but uncertainty has probably reached a peak since its inception and the situation remains very fluid. It is not surprising then that Germany has been pressing to postpone any Greek debt relief and stick to the original plan of implementing the measures only at the end of the current bailout program (i.e. next summer).

Fig. 2: Polls and coalitions since last election

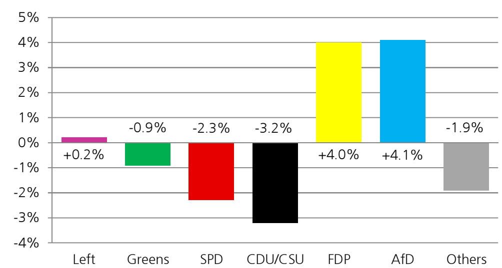
CDU-led government most likely



Note: Based on the five-poll average of various pollsters
Source: INSA, Emnid, Forsa, Forschungsgruppe Wahlen, GMS, Infratest dimap, Ipsos, Civey, Allensbach, Trend Research, UBS, as of 24 August 2017.

Fig. 3: Current polls vs. last election

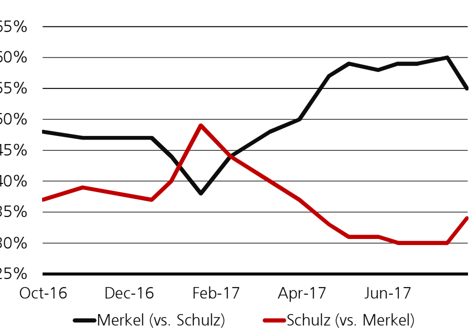
The last four years have seen a shift to the right



Note: Based on the 5-poll average of various pollsters
Source: INSA, Emnid, Forsa, Forschungsgruppe Wahlen, GMS, Infratest dimap, Ipsos, Civey, Allensbach, Trend Research, UBS, as of 24 August 2017.

Fig. 4: Chancellor's approval ratings

Angela Merkel's comeback



Note: The question posed was "who would you rather see as chancellor after the Bundestag elections…" when given the choice between Merkel and Schulz.
Source: Forschungsgruppe Wahlen: Politbarometer, UBS, as of 25 August 2017.

German manifestos and Greece

Given the underlying political trends in Germany, the implications for Greece are likely to differ depending on the CDU/CSU's coalition partner. If the CDU/CSU again teams up with the SPD, the current German policy on Greece will probably change little, as the SPD doesn't want any country pushed out of the euro. The Greens meanwhile explicitly call for debt relief for Greece, while the FDP wants Greece to exit the euro.

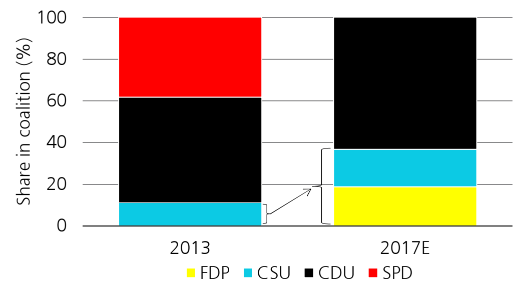
Should the election produce results that would enable the CDU/CSU to form a majority government with the Greens and/or the FDP, we would expect it to try to do so before opting for another grand coalition. What's more, the CDU/CSU would probably approach the FDP first if it has a choice between the Greens and the FDP.

A more conservative German government within reach

The FDP would likely punch beyond its weight (it currently polls 8-9%) in a conservative government. The SPD would be leaving the coalition in this scenario, so the relative importance of the FDP and CSU would increase accordingly, and together they would make up over one-third of such a coalition (see Fig. 5). The current government holds 80% of the parliamentary seats, while a CDU/CSU/FDP coalition would unlikely gain much more than 50% of them. What's more, the CDU itself boasts conservatives in its own ranks. Almost one-quarter of the CDU/CSU voted against the third Greek bailout package in the summer of 2015, counter to Merkel's clear recommendation. Adding these parliamentarians to the mix, the conservatives could easily make up half or more of the future German government. It is worth recalling that the CDU/CSU and the FDP ran the government between 2009-2013, during the euro debt and Greek crises.

Fig. 5: Potential CDU/CSU/FDP coalition

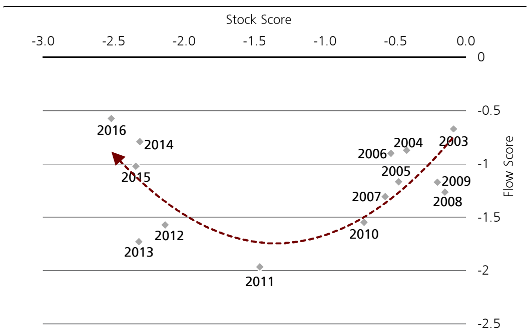
CSU and FDP would control over a third of the coalition's parliamentary seats



Note: Share of CDU, CSU, and FDP (in 2017) election of total votes received, based on five-poll moving average. Expected CSU election result based on Bavarian polls. Source: Wahlrecht, UBS, as of 24 August 2017.

Fig. 6: Greek synthetic imbalance path

Greek fundamentals have stabilized



Note: The stock dimension is based on the debt-to-GDP ratio, the net international investment position (i.e. net foreign financial position of all residents in a country) and excess unemployment. The flow dimension is based on the government deficit, the current account balance and the nominal GDP growth.

Source: UBS, Haver Analytics, as of 2016

Greece's program exit next year

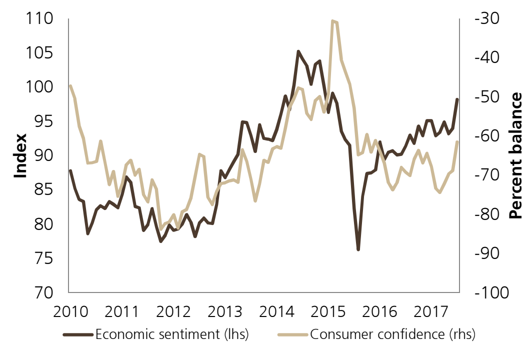
Greece: The tide is turning

With the second review of the third bailout program completed, the IMF approving a (conditional) standby arrangement for Greece and economic sentiment returning to levels last seen in early 2015, the tide is turning in Greece (see Fig. 6). European Commissioner Pierre Moscovici has already recommended releasing Greece from the EU's Excessive Deficit Procedure (before France and Spain). It is unlikely to need another formal bailout program next summer when the third one ends (unless financial market volatility soars), even if a Eurozone-sponsored standby facility will probably be necessary. We see the chances of Greece being able to issue enough new bonds to fully fund a proposed

EUR 9bn cash buffer until program end at around one in five. Funds from the existing European Stability Mechanism (ESM) program to fund this cash buffer or a new ESM-financed standby facility will therefore most likely be required and are expected to be strictly conditional (even after the program ends).

We expect the forthcoming debt relief to focus on maturities of European Financial Stability Facility (EFSF)/ESM loans being extended by 10 or more years, the aforementioned standby facility and locking in low coupons by converting floating rate into fixed rate loans. This should open up a window for Greece to tap bond markets, ideally until the extended EFSF loans come due (currently starting by 2023). To this effect, Greece issued a five-year bond totaling EUR 3bn in July, with half of the volume from a switch tender of an existing bond and half in fresh money (three years after its last bond issue in 2014). The degree of Eurozone support (i.e., the extent of debt relief and the standby facility) beyond the current bailout program will depend on the Greek economy, the upcoming German government and the success of further bond issuances before next summer.

Fig. 7: Greek economic sentiment
Sentiment boosted by end of second review



Source: UBS, Haver Analytics, as of July 2017

Fig. 8: Greek unemployment rate
Steadily improving

Source: UBS, Haver Analytics, as of June 2017

Economic conditions for Greece's bailout exit

Although the Greek economy is faring somewhat less well than we anticipated this year, it should still print growth of 1% or more. This would be its best rate since 2007. The growth would certainly have been better in the first half of the year had the second review not been so protracted (thereby creating uncertainty). Meanwhile, economic sentiment has benefited from the conclusion of the second review in the current bailout program (see Fig. 7).

With this hurdle out of the way, the economy should be able to expand by more than 2% next year, dropping the politically sensitive unemployment rate below 20% by the second half of 2018 (it peaked at 27.9% in 2013). Joblessness in the country has been falling significantly faster than in the rest of the Eurozone for a number of years (see Fig. 8). This backdrop should facilitate the bailout exit next year. Moreover, the European Commission sees the structural unemployment rate in Greece at 15.5%. Assuming no recession hits, full employment would be reached in 2021 if average progress in the labor market since 2013 is maintained.

Political backdrop for the program exit

The political outlook is more uncertain. If our base case of a grand coalition in Germany materializes, Greece should get some debt relief, opening up a window for it to tap bond markets. But the German political outlook is clouded by possible CDU/CSU coalitions with either the Greens or the FDP, which together with the CDU/CSU are polling close to 50%. As we laid out earlier, different coalitions imply different stances toward Greece. Nonetheless, even with the FDP in the government, we would still expect a Greek program exit by next year, even if debt relief measures might be lighter and conditionality on the stand-by facility tougher.

Greek snap elections unlikely next year

Political uncertainty exists in Greece as well, as a snap election could be called next year. The current Syriza government continues to lag New Democracy by 16 percentage points in the polls (see Fig. 9), even as popular support for Syriza has stabilized. Nonetheless, we think the party is hoping that signs of further macroeconomic improvement will increase its popular support. Key variables are economic growth, further private bond issuances and, most importantly, the exit from the bailout program (including the amount of debt relief).

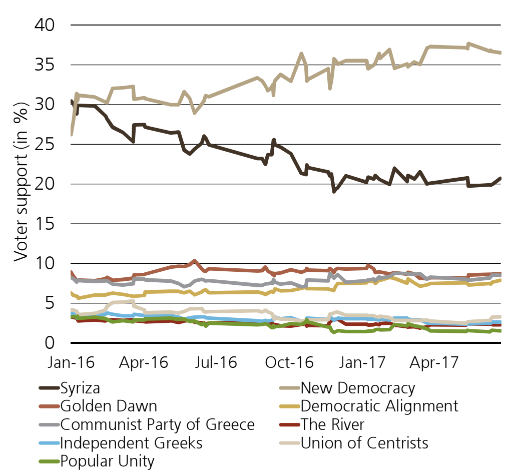
With the exit now on course for next summer, the likelihood of snap elections in 2H18 is increasing, as the Greek government might want to capitalize on political momentum afterward. In addition, the unemployment rate is on course to fall below 20% by then – most likely during the summer as well. But given the large gap the government trails New Democracy by in the polls, it might need to wait until 2019 for the improved economic environment to be fully mirrored in poll figures. We think the election is more likely to take place then, even if risks to our view have increased.

When the election does near, Greek political parties may be tempted to promise relief to the electorate as a reward for enduring tough times. But until the vote we expect the government to prioritize the bailout exit and additional bond market issues rather than deviate significantly from its fiscal targets. Furthermore, any deviations from fiscal targets should initially be muted by the post-program conditionality imposed by creditors, in our view.

The upside case

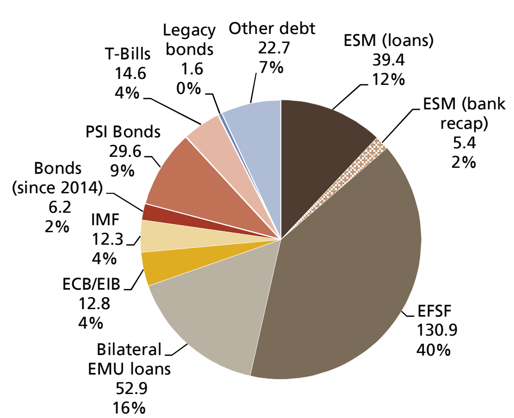
Given the high uncertainty, economic forecasts about Greece vary widely, so we see scope for upside surprises. These would likely feed into better fiscal performance and a faster fall in the unemployment rate. This backdrop could facilitate Greece's bailout program exit and help the country build a greater cash buffer via possible new bond issues. Additional government deposits could assure bondholders and rating agencies that the country could withstand a moderate economic setback without requiring immediate external assistance.

Fig. 9: Greece: political polls
Syriza has stabilized



Note: Based on the 5-poll moving average of various pollsters
Source: Metron Analysis, Marc, Alco, PAMAK, Kapa Research, MRB, Pulse RC, ProRata, Bridging Europe, Public Issue, Opinion Poll, Palmos Analysis, AUEB-STAT, Rass, UBS, as of 4 July 2017

Fig. 10: Greek government debt
In EUR bn, total debt EUR 328bn



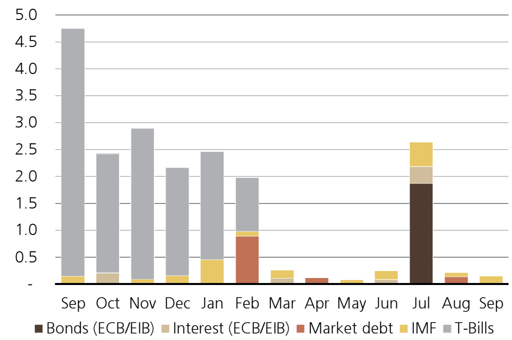
Source: UBS, IMF, ESM, Bloomberg, as of 28 August 2017.

The downside case

We consider the likelihood high that Greece will experience renewed fiscal problems and funding stress over the next five years, potentially triggered by a global recession. The many moving parts in the wider EU and the Eurozone and the likelihood of further changes of government in major countries make it almost impossible to predict how much they would support Greece in a future crisis. A greater financing gap would require negotiations about a new support program with creditors, and Greek public opinion on euro membership would likely deteriorate in the event of a renewed crisis or recession.

Fig. 11: Debt payments due until program end

In EUR bn



Source: UBS, IMF, Bloomberg, as of 28 August 2017.

Bond markets: Short versus long-term views

The ECB's potential Greek bond purchases

The European Central Bank (ECB) will closely watch the extent of debt relief granted by official sector creditors before considering whether to include Greek government bonds in its quantitative easing (QE) program. ECB purchases could amount to EUR 4-5bn before it hits its issuer limit (33%), but they will be constrained by the available instruments that meet the ECB's own eligibility criteria at the time of purchase.

To this effect, the ECB will conduct its own debt-sustainability analysis once the details of next year's debt relief are known. Its analysis will be independent of that done by the IMF, which recently deemed Greek debt unsustainable under all scenarios it considered. Since creditors consider debt relief only for the end of the bailout program (next summer), we think that the ECB will probably not rush to purchase Greek bonds. Furthermore, we believe it would rather focus on the total/cumulative share of Greek bonds in its bond portfolio when it comes to the country capital key restriction. This would mean that in any given month the ECB could buy an outsized share of Greek bonds relative to its capital key.

Bond performance will mirror ECB and primary market activity

Greek government bonds being included in ECB QE purchases and enjoying a potential temporary over-allocation would strongly support their performance. But current valuations already reflect a certain expectation of QE inclusion, so we view the final ECB decision as a binary valuation driver. In the event that the ECB does not include them, the bonds would likely suffer a sharp sell-off, and Greek access to primary markets could be challenged. The latter is important for Greece to smoothly exit the bailout program next year.

Without sufficient pre-funding ahead of the program exit and certain bond market access thereafter, Greece will likely struggle to meet its large bond payments due by 2019 (see Fig. 15). Even after the partial repurchase of its 4.75% bond due 17 April 2019, this bond has a volume of EUR 2.45bn outstanding. In addition, several older bonds held by the ECB (from the Securities Markets Program) fall due in 2019, most notably a 6% bond with a nominal value of EUR 3.74bn on 19 July 2019. In total, Greece will face 2019 nominal bond repayments of EUR 9bn and interest payments on bonds (excluding support loans and IMF dues) of EUR 1.8bn.

If Greece maintains continued bond market access, we think it will conduct further switch tender offers for bonds held by private investors and aim to collect additional fresh money to build up government deposits for future debt payments. In addition, ahead of the bailout program exit, it will likely also aim to draw remaining loan capacities from the ESM and keep them as cash reserves. This strategy was also followed by Portugal and Ireland ahead of their program exit and is crucial to its success, in our view.

Longer-term considerations for bondholders

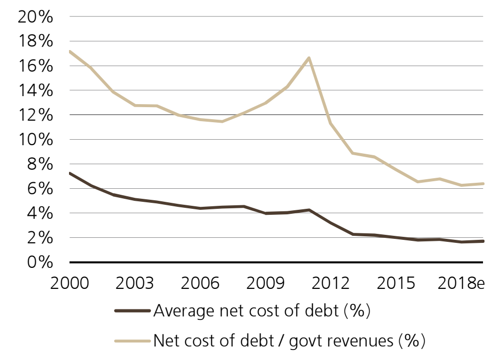
Long term, Greece's recovery is unlikely to be a one-way path like the longer-term budget plan figures of the current support program suggest. Few countries, usually large commodity producers like Norway, have achieved sustained high primary fiscal surpluses. Since Greece's first bailout in 2010, fiscal plan targets have been missed and corrected sharply several times, so we think it prudent to look at current longer-term plan targets with some caution. Even including the proposed debt-relief measures, Greece will need to allocate considerable funds to servicing its debt, currently 6.8% of government revenues (see Fig. 12), and more private-market funding will increase the average cost of its debt. Keeping the overall budget deficit in check and consolidating the large debt burden requires a significant primary surplus.

Fiscal surpluses are challenged by economic recessions (which are usually not considered by fiscal forecasts until they occur) and domestic political needs. The latter may become a main challenge after the next election.–The substantial reforms of recent years have all been enforced by external creditors (IMF, Eurogroup, ECB), under the threat of default and/or a euro exit, so it appears unlikely that the Greek government will stay on a strict reform path once it no longer depends on funding from these official sector creditors.

Greece is no different from any other country in this respect.

Fig. 12: Greek cost of debt are bottoming

IMF forecasts suggest slight increase from 2018



Source: UBS, IMF as of 22 August 2017

Unlike its peers though, it carries a huge debt load of 181% of GDP, so that signs of fiscal deterioration can cut it off from affordable bond market funding again. After exiting the support program, the Greek government would likely hesitate to formally request renewed external funding, even if a standby facility had been agreed, because of the potential conditionality that would be imposed by creditors and the domestic political costs of having to admit failure at operating independently again.

Rating and capital control considerations

While an exit from the euro is not our base case, it is sufficiently likely to constrain the credit profile of the country to ratings in the B/CCC category, in our view. Greece is currently rated Caa2, positive by Moody's, B-, positive by S&P and CCC by Fitch. If the country exited the euro, its government bonds would default and the recovery value of bond market debt would likely be very low. Official sector creditors might be better positioned to recover part of their claim. Should our upside scenario materialize, with Greece building a significant cash buffer for future debt payments and potential budget shortfalls, credit ratings could be upgraded further, potentially toward the high B category.

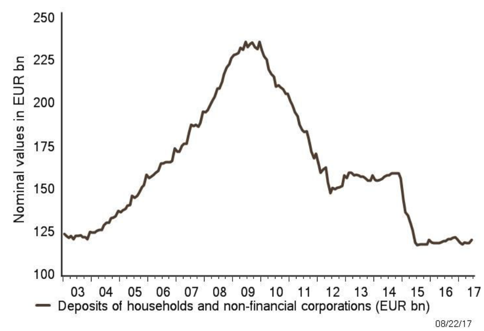
Without an investment grade rating, Greek government bonds would not be eligible for Eurosystem monetary operations without a waiver from the ECB. When the ECB announced on 3 May 2010 that it would apply a waiver for Greek government bonds (so that Greek banks could continue to fund themselves in the Eurosystem), it was based on the bailout program. With Greece exiting this program next summer, the waiver is in principle set to expire. If the standby facility for Greece is (at least initially) structured as an Enhanced Conditions Credit Line (ECCL) from the ESM, the waiver may remain in place for up to two years after the end of the bailout program. If that doesn't work, we would expect Greek financial institutions to be able to access central bank money through the Bank of Greece's Emergency Liquidity Assistance. With the uptrend in bank deposits yet to emerge (see Fig. 13), we think therefore that a full lifting of capital controls is unlikely in the short term.

Investment conclusions

Greek bond yields have increased somewhat since the late July bond issue (see Fig. 14), and we think Greece will refrain from issuing long-dated bonds at current yields. Considering the debt maturity profile (see Fig. 15), further new issues will focus on tenors ranging from 2020 to a maximum of 2025, in our view.

Fig. 13: Greek bank deposits

Clear uptrend yet to emerge



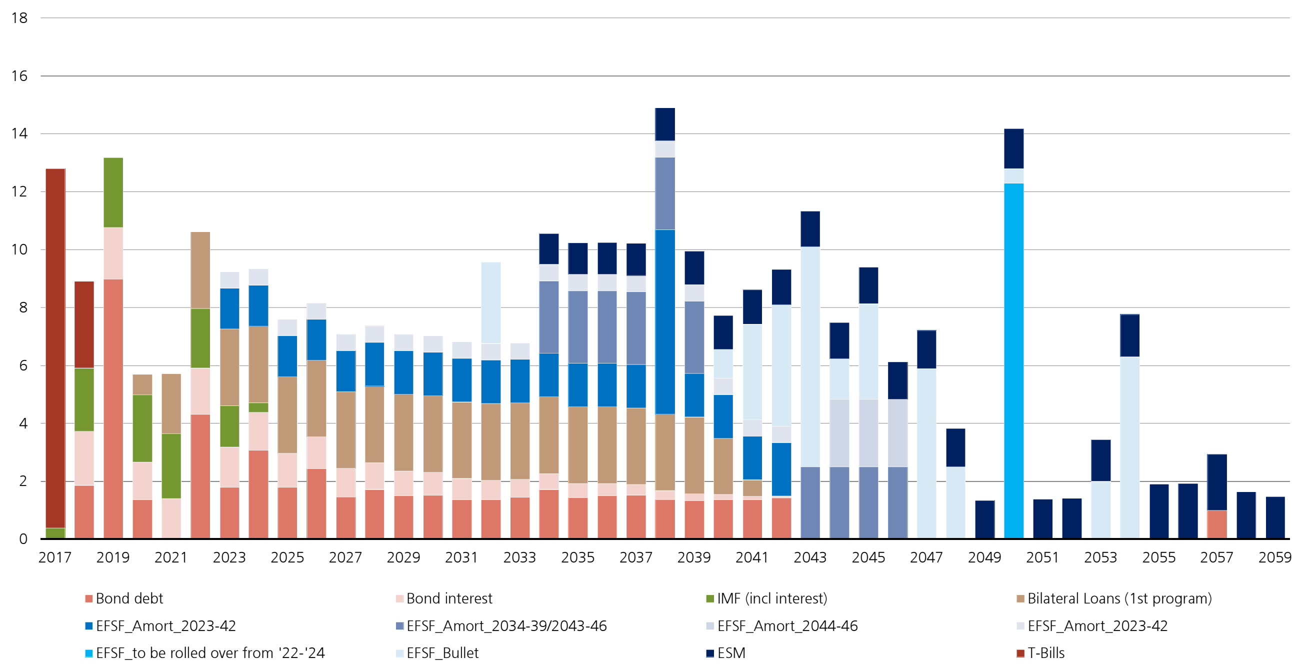
Source: Haver Analytics, UBS as of June 2017

Fig. 14: Greek 10-year bond yields

in %, compared to German Bunds

Source: Bloomberg, UBS as of 28 August 2017.

Fig. 15: Greek debt maturity profile ahead of potential debt re-profiling measures
Amounts in EUR billions



Source: UBS, ESM, IMF, Bloomberg, as of 28 August 2017.

Appendix 1: European political calendar

Fig. 16: European political calendar
Greek elections to take place alongside changes at the helm of Europe's most important institutions

	Country/area	Event/institution	Officeholder
Sep 2017		German Bundestag election	–
2H 2017		Eurogroup President	Jeroen Dijsselbloem (NL)
Jan 2018		European Investment Bank President	Werner Hoyer (DE)
1H 2018		Italian parliamentary election	–
May 2018		ECB Vice President	Vítor Constâncio (PT)
Dec 2018		ECB Banking supervision (SSM)	Danièle Nouy (FR)
Mar 2019		Brexit	–
Apr 2019		ECB Council/Bundesbank President	Jens Weidmann (DE)
May/Jun 2019		European parliamentary election	–
Oct 2019		ECB President	Mario Draghi (IT)
Oct 2019		Greek parliamentary election	–
Oct 2019		European Commission President	Jean-Claude Juncker (LU)
Nov 2019		European Council President	Donald Tusk (PL)

Source: UBS CIO WM, as of August 2016. Note: Dates for officeholders refer to end date of respective mandate.

Appendix 2: Electoral programs for the German elections

	CDU/CSU	SPD	FDP	Greens	Left Party	AfD
Taxes and fiscal	• Income tax: Raise the 42% upper tax rate threshold from €56k to €60k (€15bn per year). • Solidarity tax: Abolish in steps from 2020 (€4bn per year from 2020). • No tax hikes, no wealth tax, no inheritance tax change. • Fiscal rules: Commitment to balanced budget and constitutional debt brake. • Support Financial Transactions Tax (FTT).	• Income tax: Raise the 42% upper tax rate threshold from €56k to €60k (€15bn per year). • Income tax: New 45% tax rate will kick in at €76.2k with a 3% surcharge for incomes above €250k (€10bn per year). • Solidarity tax: Abolish for lower incomes from 2020 (€10bn per year from 2020). • Close loopholes in inheritance tax and VAT. • Support FTT.	• Income tax: Unspecified income tax cuts and indexation of thresholds. • Solidarity tax: Completely abolish from 2020. • No tax hikes, no wealth tax, no inheritance tax change. • Fiscal rules: Balanced budget insufficient, actual debt reduction targeted. • Debt: Insolvency law for federal states and municipalities. • Lower energy tax.	• Income tax: Increase in the tax free allowance, higher tax rate for >€100k incomes. • Wealth tax. • Corporate tax: salaries >€500k not tax deductible. Fighting corporate tax evasion or avoidance. • Support FTT.	• Income tax: Raise tax free threshold to €12,600 per year. Raise income tax for incomes above €7,100 per month. • Introduce wealth tax from €1 million.	• Income tax: Tax-bands instead of tax rate progression and indexation of thresholds to avoid "cold progression". • Income tax: Increase the tax-free minimum income. • VAT cut by 7ppt. • Reduce tax quota in the medium-term to 40%, from nearly 50% in 2016. • Abolition of inheritance tax and no introduction of wealth tax. • Country-of-origin principle for corporate taxation.
Welfare and pensions	• Increase in child benefits (€300 per child per year). • Childcare: Right to full-time primary schools. • Pensions: No change. Commission to make proposals for post-2030 pensions by 2019.	• Social security subsidies for low-income households. • Equal employers/ employees social sec. contr. (€5bn/year). • Social security: Same healthcare insurance for all. • Childcare: Abolishing nursery fees. Full-time primary schools. • Families: €300 p.m. for parents if both are working part-time. • Pensions: Replacement ratio of 48%, maximum contributions of 22%; "Solidarity pension"; keep pension age unchanged.	• Flexible pension age (60-70) with adjusted pension payments. Improve possibilities to earn on top of pension. • Social security exemption of second-pillar pensions and less regulation of investment spectrum of third-pillar pensions. • Education: Introduce university tuition fees (paid after graduating).	• Pensions: New minimum pension. Stabilise replacement ratio. Retirement age stays at 67, but early retirement from 60 possible. Improve possibilities to earn on top of pension. All companies have to offer second pillar pensions. • Social security: Same health and care insurance for all. • Social subsistence: increase in allowances.	• Raise replacement ratio from 48% to 53%. • Minimum pension of €1,050 per month. • Equal pensions in East and West Germany. • Minimum welfare payment of €1,050 per month. • Same health insurance for all.	• Full pension after 45 years of contributions. • Pensioners can earn additional income without reductions of their pensions. • Harmonization of employer and employee social security contributions.
Public investment and spending	• Raise investment in R&D from 3.0% of GDP to 3.5%. • More investment in digital infrastructure (no amounts). • 15k new police officers. • Raise military spending to 2% of GDP by 2024.	• "Investment offensive": Raise public investment by €30bn over 4 years. • Raising investment in R&D from 3.0% of GDP to 3.5%. • 15k new police officers. • Rejection of 2% of GDP military spending.	• Raise education expenditure as share of GDP to Top 5 of OECD (from 3.7% of GDP to 5.6% of GDP according to the OECD 2013). • €2bn per year extra for roadbuilding (for 20 years). • More investment in digital infrastructure (no amounts).	• Major investment in renewable energy. Aim 100% renewables by 2030 (no amounts). • Additional investment in education (no amounts). • More investment in digital infrastructure (no amounts).	• Additional public investment in healthcare, transport, housing construction, energy, digital infrastructure (no amounts). • Expansion of public sector employment (no amounts). • Ending privatizations.	• Additional investment in transport infrastructure and education (no amounts).
Immigration and refugees	• New skilled immigration law. • No cap on refugee intake.	• New skilled immigration law. • No cap on refugee intake.	• New immigration law. • Dual citizenship.	• New immigration law. • Citizenship: by place of birth, no restriction on dual citizenship.	• No limits to asylum. • Major investments and legislative action to improve integration of immigrants.	• Immediate closure of borders for immigration. • Outlawing some symbols of Muslim faith in public.

	CDU/CSU	SPD	FDP	Greens	Left Party	AfD
Housing	• 1.5 million new flats 2017-2021: streamlining planning permissions, introducing regressive depreciation. • New home buyer subsidy (€1,200/year per child)	• Better enforcement of the rent brake. • Indexation of rent subsidies. • More flats in public or company ownership.	• Increase annual depreciation from 2 to 3% to promote housebuilding.	• 1 million new flats with low rents. • Better enforcement of the rent brake.	• 250k new flats per year with regulated rents.	• Reduction of house purchase taxation. • Streamlining of planning permissions.
Labour Market	• Flexibility in weekly working hours. • Halving unemployment to 1.25 million by 2025.	• Longer unemployment benefits and wider eligibility. • Temporary work: Equal pay from day 1; new restrictions. • Wages: fewer minimum wage exceptions; strengthened collective bargaining. • Worker board representation threshold lowered to 1,000 employees.	• Deregulation of temporary jobs. • Increased working time flexibility	• Wages: fewer exceptions from minimum wage. • Temporary work: new restrictions to avoid abuse. Equal pay from day 1. • Sabbatical: new time-out for social care with government bursary.	• Raise minimum wage from €8.50 per hour to €12. • Abolition of temporary work contracts. • Reduction of working hours. • Raise wages in social sector. • Equal pay of men and women. • Longer unemployment benefits.	• Supports minimum wage. • Use of temporary work limited to 15% of the workforce per company. • New citizens' work service for the long-term unemployed. • Reform of labor statistics to reflect full extent of unemployment.
Eurozone and EU	• European Monetary Fund (EMF) to aid Eurozone countries in trouble. • Debt mutualization ruled out. • Focus on EU defense union. • Corporate tax harmonization with France. • No Turkish EU accession.	• European infrastructure investment program. • More flexible Eurozone fiscal rules. • European social union (common welfare standards and employee representation). • Coordinated Eurozone economic policy. • EZ budget, funded by FTT. • Convert ESM into EMF. • No country should be forced to exit the euro. • EU tax harmonization. • European defense union. • Replacement of UK MEPs with transnational lists. • New attempt at EU constitution.	• "Europe of different speeds". • European Army. • Phasing out of the ESM. • ECB should not complement ESM programs (OMT). • Insolvency law for Eurozone member states. • New possibility for orderly exit from Eurozone. • Banking: Risk weights for sovereign bonds, strict bail-in enforcement. • Automatic sanctions in stability and growth pact. • End to low ECB interest rates. • Turkey: end of EU accession negotiations.	• European refugee policy. • Free Interrail-Ticket for 18-year-olds. • Europe of different speeds must be exception. • Debt relief for Greece. • "New Green Deal" for Europe. New investment fund. • Minimum standards for welfare and labor law. • Stronger EU parliament. • EU defense union. • Turkey should keep EU accession option.	• End of austerity and no threat against EZ countries pursuing alternative economic policies. • Referendums on treaty changes. • Repeal of CETA et al. • Investment program • Direct ECB government funding. End independence. • Restructuring of "illegitimate" public debt, including Greek debt restructuring, with Germany unilaterally paying war reparations to Greece. • Rejection of capital markets union. • European minimum wage at 60% of the national average wage.	• Conversion of EU into looser grouping of states by abolishing the Maastricht and Lisbon treaties. • Germany to exit EU if other member states disagree. • Outlawing ECB asset purchases and zero or negative interest rates. • No bail-outs for states and banks, no banking union. • Even before "D-Exit" from euro, end Target 2 imbalances. • Preparation of return to Deutsche Mark. • No European army. • Ending bilateral free trade deals like Ceta.
Brexit	• Limit damage of Brexit for people and the economy. • Countries leaving EU no longer benefit from its advantages.	• No cherry-picking, no division of the EU. • Principles of single market are non-negotiable.	• No cherry-picking • Principles of single market are non-negotiable. • No extension of Article 50. • Open EU door for Scotland.	• Priority for unity and integrity of the EU, no cherry-picking. • Help for Northern Irish and Scottish "Remainers" • Principles of single market are non-negotiable. • UK citizens in Germany should have easy way to German citizenship.	• Maintaining mutual free mobility of labor and expats rights.	• Brexit as a role model: use threat to leave the EU and Eurozone to reform the EU.

Other	• Outlawing online pharmacies.	• More financial regulation, including support for bank leverage ratio and separation of retail and wholesale banking.	• Venture-Capital-Law to end tax preference of debt over equity. • Liberalization of transport (Uber) and hospitality (AirBnB). • Privatization of rail operator. • Flexibility in opening hours, including Sunday.	• More financial regulation, including support for bank leverage ratio and separation of retail and wholesale banking.	• Foreign policy: Abolition of NATO, better relations with Russia.	• Direct democracy: Introduction of referendums; direct election of federal president. • Social: End of antidiscrimination law, opposition to same-sex marriage. • Foreign policy: Improved relations with Russia; exiting Paris climate agreement. • Energy: Continued use of nuclear energy.

Source: UBS CIO WM, Citi Research, as of July 2017. Note: Manifesto of Greens not final yet.

Glossary

Bank Recovery and Resolution Directive (BRRD)
The BRRD harmonizes the tools used in the recovery and resolution of credit institutions in the EU. It stipulates that, should a bank fail, its shareholders and creditors should normally be first in line to absorb any risks and losses. Only then should a resolution fund financed by the entire banking industry (Single Bank Resolution Fund, or SBRF) step in. In extreme cases, government institutions can still be financially involved in the recovery or resolution of an institution ("bailout").

Current account
The current account measures the cross border flow of goods, services, net investment income and cash transfers in a given period. Usually, the trade balance is the largest component of the current account. A current account surplus (normally associated with a trade surplus) means that the respective country has increased its net foreign assets, or in the case of net liabilities, reduced it in a specific period.

Deposit Guarantee Schemes Directive (DGSD)
The new European DGSD entered into force on 2 July 2014. It replaced the previous one from 1994. Its main elements include: simplification and harmonization, in particular relating to coverage and payout arrangements; further reduction, to one week, of the time limit for paying out depositors, and better access for DGSs to information about their members (i.e. banks); harmonization of minimum ex ante financing requirements for DGSs; mutual borrowing between DGSs, i.e. a borrowing facility in certain circumstances.

ECB Deposit Facility
A standing facility of the Eurosystem which counterparties may use to make overnight deposits at a national central bank. Such deposits are remunerated at a pre-specified interest rate ("deposit rate").

ECB Executive Board
One of the decision-making bodies of the ECB. It comprises the president and vice-president of the ECB and four other members, all of whom are appointed by common accord by the heads of state or government of the EU member states whose currency is the euro.

ECB Governing Council
The supreme decision-making body of the ECB. It comprises the president and vice-president of the ECB plus the other members of the Executive Board and the governors of the national central banks of those EU member states whose currency is the euro.

ECB longer-term refinancing operation (LTRO)
A regular open market operation executed by the Eurosystem in the form of a reverse transaction. Longer-term refinancing operations are carried out through monthly standard tenders and normally have a maturity of three months.

European Fund for Strategic Investments (EFSI)
An investment plan from the European Commission aimed at relaunching public and private investment in the real economy over 2015–2017. The fund is operated by the European Investment Bank.

European semester
A six-month period each year when member states' budgetary, macro-economic and structural policies are coordinated so as to allow member states to take EU considerations into account at an early stage of their national budgetary processes and in other aspects of their economic policymaking.

European Stability Mechanism (ESM)
The ESM is an intergovernmental institution based in Luxembourg, set up to provide financial assistance to Eurozone member states experiencing, or being threatened by, severe financing problems, if this is indispensable for safeguarding financial stability in the Eurozone as a whole. The maximum lending capacity of the ESM is set at EUR 500bn. This is achieved with a subscribed capital of EUR 700bn (EUR 80bn paid-in capital, the rest callable). The ESM entered into force on 27 September 2012. It took over the tasks fulfilled by the European Financial Stability Facility (EFSF).

European System of Financial Supervision (ESFS)
The group of institutions in charge of ensuring the supervision of the EU's financial system. It comprises the European Systemic Risk Board, the three European Supervisory Authorities (the European Banking Authority, the European Securities and Markets Authority and the European Insurance and Occupational Pensions Authority), the Joint Committee of the European Supervisory Authorities, and the national supervisory authorities of the EU Member States.

European Systemic Risk Board (ESRB)
An independent EU body responsible for the macro-prudential oversight of the financial system within the EU. It contributes to the prevention or mitigation of systemic risks to financial stability that arise from developments within the financial system, taking into account macroeconomic developments, so as to avoid periods of widespread financial distress.

Eurosystem
The central banking system of the euro area. It comprises the ECB and the national central banks of those EU Member States whose currency is the euro.

Excessive Deficit Procedure (EDP)
The corrective arm of the Stability and Growth Pact (SGP) ensures that member states adopt appropriate policy responses to correct excessive deficits by implementing the Excessive Deficit Procedure (EDP). The EDP operationalizes the limits on the budget deficit and public debt given by the thresholds of 3% of deficit to GDP and 60% of debt to GDP not diminishing at a satisfactory pace.

Full allotment policy
This policy provides banks with access to unlimited ECB liquidity, as long as eligible collateral is delivered to the ECB. The MRO interest rate applies to the liquidity lent out under fixed allotment policy.

HICP Inflation
Consumer price inflation in the euro area is measured by the Harmonized Index of Consumer Prices (HICP). The HICP is compiled by Eurostat and the national statistical institutes in accordance with harmonized statistical methods. The headline inflation refers to the inflation rate including core and non-core inflation.

Main refinancing operation (MRO)
A regular open market operation executed by the Eurosystem (in the form of a reverse transaction) for the purpose of providing the banking system with the amount of liquidity that the former deems to be appropriate. The interest rate on MROs represents the key policy rate for the ECB to implement its monetary policy stance.

Marginal lending rate
The interest rate on the Eurosystem's marginal lending facility which banks may use for overnight credit from a national central bank that is part of the Eurosystem.

Monetary aggregate
Currency in circulation plus outstanding amounts of certain liabilities of monetary financial institutions (MFIs) that have a relatively high degree of liquidity and are held by non-MFI euro area residents outside the central government sector. The Governing Council has announced a reference value for the growth of M3.

Outright monetary transactions (OMT)
A program under which the ECB makes purchases ("outright transactions") in secondary, sovereign bond markets, under certain conditions, of bonds issued by Eurozone member states. Conditions for eligibility are that the government has asked for financial assistance through the ESM or EFSF and that it agrees to implement certain domestic economic measures.

Purchasing Manager Index (PMI)
The Markit PMI™ series are monthly economic surveys of carefully selected companies compiled by Markit. They provide advance insight into the private sector economy by tracking variables such as output, new orders, employment and prices across key sectors.

Securities Markets Programme (SMP)
Interventions by the Eurosystem in public and private debt securities markets in the Eurozone to ensure depth and liquidity in those market segments that are dysfunctional. The objective is to restore an appropriate monetary policy transmission mechanism, and thus the effective conduct of monetary policy oriented toward price stability in the medium term.

Single Resolution Mechanism (SRM)
The SRM complements the Single Supervisory Mechanism. It is set to centralize key competences and resources for managing the failure of any bank in the Eurozone and in other member states participating in the banking union.

Single Supervisory Mechanism (SSM)
The SSM is a new system of banking supervision for Europe. It comprises the ECB and the national supervisory authorities of the participating countries. Its main aims are to ensure the safety and soundness of the European banking system, increase financial integration and stability, and ensure consistent supervision. The SSM is one of the two pillars of the EU banking union, along with the SRM.

Six-pack
A set of six legal acts adopted in 2011, strengthening procedures for the surveillance of the member states' fiscal policies (the "Stability and Growth Pact") and introducing new ones for their macroeconomic policies. The aim is to better control public deficits and national debt and to better address macroeconomic imbalances.

Stability and Growth Pact (SGP)
The SGP is a rule-based framework for the coordination of national fiscal policies in the EU. It was established to safeguard sound public finances, based on the principle that economic policies are a matter of shared concern for all member states.
TARGET2
The second-generation TARGET system. It settles payments in euro in central bank money and functions on the basis of a single IT platform, to which all payment orders are submitted for processing. This means that all payments are received in the same technical form.

Targeted Long-Term Refinancing Operations (TLTRO)
A new LTRO (see above) announced on June 2014 targeted at business loans, consisting of eight LTROs. Its aim is to improve bank lending to the Eurozone non-financial private sector in order to ensure that the supply of credit will not endanger the recovery of the real economy. TLTROs should also improve the distortions in the monetary transmission channel. TLTROs have been accessible on a quarterly basis from September 2014.

Treaty on stability, coordination and governance (fiscal compact)
The fiscal compact is an intergovernmental treaty signed by euro area members and other EU member states at the European Council meeting on 2 March 2012. The treaty requires structural government deficits not to exceed 0.5% of GDP and the budget to be in balance or surplus. In addition, debt to GDP ratios above 60% of GDP must be reduced over a 20- year period (subject to a three-year grace period following compliance with the deficit objective).

Two-pack
The second package of proposals on economic governance was presented by the Commission in November 2011 and builds on the so-called "six-pack" of economic governance proposals. Once adopted, the two draft regulations will introduce provisions for enhanced monitoring of Eurozone countries' budgetary policies.

Unit labor costs (ULC)
ULC measure the average cost of labor per unit of output and are calculated as the ratio of total labor costs to real output. A rise in an economy’s unit labor costs represents an increased reward for labor’s contribution to output.

Source: BaFin, Bundesbank, ECB, European Union, Markit, OECD.

Appendix

Terms and Abbreviations

Term / Abbreviation	Description / Definition	Term / Abbreviation	Description / Definition
A	actual i.e. 2010A	COM	Common shares
E	expected i.e. 2011E	Shares o/s	Shares outstanding
UP	Underperform: The stock is expected to underperform the sector benchmark	CIO	UBS WM Chief Investment Office