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SUBJECT: Germany and the European economic crisis

SOURCE: Sources with excellent access to the highest levels of the European political and security communities.

THE FOLLOWING INFORMATION COMES FROM AN EXTREMELY SENSITIVE SOURCE AND SHOULD BE HANDLED WITH CARE.

1. During the evening of May 6, 2012 German Minister of Finance Wolfgang Schaueble initiated a secure conference call with Chancellor Angela Merkel to discuss the election of Socialist Francois Hollande as President of France. According to a knowledgeable source, Merkel acknowledged that Schaueble’s predictions regarding the French elections were borne out, and congratulated him on initiating low key negotiations in April 2012 between his private associates and French Socialist Party officials who will be advising Hollande, in an effort to avoid public policy debates that can only serve to undermine the position of the European Union (EU) in the current economic crisis.

2. For his part, Schaueble reminded Merkel that Hollande is first and foremost a politician, and they will have to wait and see if his actions match his rhetoric. Schaueble was pleased that Hollande stated in his acceptance speech that he wanted only to amend the current debt resolution document to include language about growth. The Germans had feared that he might demand that they renegotiate the entire agreement. The Chancellor and the Minister agreed that Hollande’s commitment to government spending to stimulate growth will encourage those in other member governments who oppose the German demands for increased austerity on the part of the Eurozone states. Schaueble noted that this situation will not only affect the EU, but will also complicate German internal politics. Merkel stated that while she had often found Sarkozy annoying, dealing with Hollande, whose entire career has been focused on French internal political battles, will be a challenge.

3. According to extremely sensitive reporting, Schaueble also pointed out to Merkel that the apparent rejection of the austerity coalition by Greek voters will only serve to confuse the world financial markets and encourage Hollande, who, as a dedicated European Socialist, sees himself as the potential new leader of the Eurozone and EU; with France showing the way out of the current crisis through a mixed economic policy led by the Socialist Government. Schaueble added that, as Merkel prepared for her first post election discussion with the French President; she must remember that he will be anxious to establish a strong position early on in their relationship. The French parliamentary elections will take place in late June and the Socialists are counting on the support of the communist led Left Front (FG) to gain control of the national legislature. According to sensitive reporting from the German External Intelligence Service (Bundesnachrichtendienst-BND), in return for FG support, Hollande promised FG leader Jean-Luc Melenchon that he would stand behind his pledge to fight German driven economic austerity measures, increase taxes on industry and wealthy citizens, while pressing for government driven stimulus programs. (Note: The FG controls between 10 and 15 percent of the vote in France, and is crucial to the Socialist success.)

4. In the opinion of this individual, Merkel noted that Hollande had issued a direct challenge to Germany, by name, regarding the balance between austerity programs and economic/job growth driven by government spending. Schaueble warned Merkel to maintain Germany’s position regarding the need for continuing austerity throughout the EU. The Minister stated that German diplomats and intelligence officers throughout Europe and at the EU Headquarters in Brussels are convinced that Hollande will maintain his commitment to the Socialist position. Merkel, for her part, added that in anticipation of this effort by Hollande, her Chancellery economic advisors have asked her to consider accepting new policy language, in very general terms, calling for an increased commitment to economic growth and an improved employment situation. Schaeuble urged Merkel, in the strongest terms, to avoid any position that does not also emphasize the need for continuing austerity measures. In the opinion of this individual, a reduction in austerity measures by Greece, Italy, Spain, and even France will lead to a crisis of serious proportions; one that will also affect the German nation.

5. (Source Comment: Speaking in strict confidence, Schaueble again stated that Merkel must remember that Hollande is a true European Socialist, whose entire career has been focused on internal French politics. The Minister believes that Hollande will initiate government spending programs, and increase taxes on wealthy citizens in an effort to stimulate economic growth and reduce unemployment. He added that in the discussions with Hollande’s advisors, officers from the Ministry of Economics learned that Hollande believes that the EU cannot wait for economic growth in the United States to stimulate growth in Europe. According to this source, Hollande believes that German internal policy must change, allowing for slight increases in inflation and a reduction in the value of the Euro. These French Socialist advisers also believe that German employers must increase the salaries of their workers, even if this involves government subsidies to allow these increases. Schaeuble added that Hollande is unconcerned by the prospect of a fall in the value of the Euro. According to this source, Hollande believes a decrease in the value of the Euro will serve the same purpose as devaluation did for European currencies under pressure in the years before the creation of the Eurozone currency union. )

6. At the same time, a particularly sensitive source noted that Schaeuble is extremely concerned over the long term affect the French elections may have on German internal politics. Although Merkel continues to be quite popular, her center-right coalition of the Christian Democratic Union/Christian Social Union (CDU/CSU) and the Free Democratic Party (FDP) is losing support across the country, with the FDP in danger of losing their seats in the German parliament (Bundestag). On the same day as Hollande’s victory, voters in the longtime CDU/FDP stronghold of Schleswig-Holstein gave 52-48 percent margin of victory to a coalition of leftist parties, with links to the French Socialist Party. The new state government includes the Social Democratic Party (SDP), the Green Party, and the far left Pirate Party. Schaueble is concerned that Hollande’s victory will give heart to other Socialist politicians in Germany as they prepare for the next scheduled national elections in 2013.

7. (Source Comment: Schaueble added that he may encourage Merkel to call early elections, if it appears that this leftist, anti-austerity movement is taking hold in Germany; in an effort to act before the opposition becomes too strong.)

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