What would Ludwig Erhard Say? *Energy Savings Obligations are viewed with a critical eye in Germany. Some even refer to them as central planning. In reality, they are well aligned with the principles of a social free market economy.*

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Nearly 35 years have passed since I came to Germany in the mid-70s to study Ludwig Erhard's Wirtschaftswunder–or "economic miracle"–at the University of Tübingen. As life would have it, my career has now brought me back to monitor Germany's Energiewende to a non-nuclear, decarbonized power sector. And the vision of Ludwig Erhard, which originally drew me here, is ever so alive today.

The success of Germany's Energiewende is dependent to a large degree upon the success of its energy efficiency policies, and how they can perhaps once again foster the intelligent interaction between market regulations and market forces that characterizes a social market economy. Yet why should the unwieldy topic of energy efficiency, of all things, be the driving force of a new social market economy, the next German Wirtschaftswunder?

The significance of energy efficiency for the Energiewende is unchallenged. However, to me the greatest lesson learned from Erhard's policies is this: An increase in energy productivity through greater efficiency is critical to any economic stimulus strategy in our current economic crisis.

One policy instrument for increasing energy efficiency is now the focus of debate over the European Energy Efficiency Directive: the so-called energy savings obligation. Although mandatory energy savings obligations have been successfully implemented in well over 30 countries, states and regions, Germany simply rejects the idea. The harshest critics in the land of Ludwig Erhard call this "central planning" of the economy. However, in reality, the concept of energy savings obligations has strong parallels with Erhard's ideas-- it is a concept well-suited to launching a new economic *efficiency* miracle.

First of all, similar to Erhard's policy framework, the goal is to "increase the pie" rather than shrink it by stimulating growth via increased productivity. In Erhard's day, the focus was on increasing labor productivity. Today, it is also about increasing energy productivity.

While Erhard was a passionate proponent of a competitive marketplace, he recognized the need to assign increased productivity a value or worth in the market. To this end, he set out to purposefully manage the volume of currency with which goods and services are purchased, and with which workers are ultimately paid. This was accomplished by controlling the money supply via the Central Reserve Bank in a way that recognized that the volume could and should be permitted to grow – but only with a clear linkage to productivity increases.

Just as the Euro and Cent serve as the "currency" for the exchange of general goods and services, kilowatt hours and units of thermal heat (or therms) serve as the "currency" for energy services such as light, heat or pumping. Similar to Erhard's aim, energy savings obligations also create a link between the volume of "currency" and an increase in productivity, that is, the more effective use of kilowatt hours and therms in the economy.

The assertion that the EU Commission's target of a 1.5% annual increase in energy efficiency represents administrative limits to economic growth is simply incorrect. Quite the opposite is true. The 1.5% is not a strict cap on energy consumption, but rather sets the annual target for increasing energy productivity. By the same token, the European Central Bank's goal of achieving a 2% inflation rate does not limit economic growth.

Second, in the case of both Erhard's market economy and an energy savings obligation, one specific agent is made responsible for the results. Following in the footsteps of successful market economies, Erhard institutionalized the role of the *Bundesbank* (German Federal Reserve) as the agent controlling the currency in circulation. Similarly, an energy savings obligations designates an agent (or agents) responsible for meeting the goal of continuously increasing energy productivity in the economy through market-based incentives. Different possibilities come to mind: In California and Denmark, it is the grid operators, in the State of Vermont, it is an institution created expressly for this purpose—each are tasked by the government with ensuring that the targets are achieved in the market.

Third, under both approaches, a public budget is strategically invested by the responsible agent to stimulate private market activity and private investment. And in the end, consumers will have more disposable income available to them, since the public investment leverages much more value added to the benefit to all consumers. Consistent with Erhard's way of thinking, the investment of public funds in energy efficiency makes particularly good sense, since it serves to remove market barriers that can effectively leverage increased private investment. Past observations suggest that this is indeed the case: Experience indicates that efficiency measures produce over their lifetime a return of three to five times on the public funds expended.

There are many available "patterns" to select from in designing an energy savings obligation, and it is time to take needle and thread out of the drawer to tailor an energy efficiency policy that best fits Germany. The express rejection of energy savings obligations as a central planning instrument certainly shows that Germany has strayed from Ludwig Erhard's insights. More importantly, by doing so Germany is missing out on an extraordinary opportunity: the opportunity of creating an "economic efficiency miracle".