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Current Issues
Business cycle

Focus Germany

Stronger growth and wages – little reaction from savers

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Germany: Taking the leap of faith; raising 2015F GDP growth to 2%. The Q4 GDP details corroborate that the German economy ended 2014 on a high note (+0.7% qoq vs +0.1% in Q3) as private consumption received a substantial stimulus from the drop of the oil prices. We increase our 2015 GDP forecast to 2.0% from 1.4% previously. This is especially due to the much larger carry-over effect courtesy of the marked Q4 GDP growth. In addition, we raise our Q1 GDP forecast to 0.5% qoq as the renewed oil price drop will boost consumption again. Sentiment also improved further in January/February with ifo expectations and the composite PMI pointing to 0.5% and 0.4% growth, respectively.

Minimum wage boosts compensation in 2015. Given the unusually positive labour market situation and the very robust outlook, negotiated wages are poised to increase by roughly 3% again in 2015. With their close to 4 million employees and agreement of a 3.4% pay rise in early 2015, the metal and electrical engineering sectors are likely to have set the benchmark. Most of the demands made to date call for wage hikes of over 5%. The minimum wage will probably tend to exert upward pressure on negotiated wages in the medium term. Moreover, it will give the overall wage level a one-off boost. German unit labour costs are likely to increase noticeably in 2015.

Is the ECB spoiling the Germans' appetite for saving? Deposit rates in Germany have fallen below 0.5%. Bund yields are negative for maturities of up to 6 years. Nevertheless, Germany's households' savings ratio appears to have hardly reacted to this. Surveys and our simple econometric model to explain saving show that interest rates do not have a significant influence on savings decisions. All the same, the savings ratio is expected to decline over the next few years. This is initially because of the effect of continually rising construction investment and prices. In the medium term, however, the dissaving of the retired baby boomers will be the decisive factor in the continued decline in the savings ratio.

The view from Berlin. Notwithstanding the SPD's clear victory and the CDU's deep fall in the recent state election in Hamburg, we do not see fundamental changes in Germany's political landscape. Chancellor Merkel's popularity has stayed high, as the majority of Germans embrace her main principles on euro-area policy, i.e. fiscal support only in return for reform efforts. For the future much will depend on the smaller parties. In Hamburg the AfD passed the 5% threshold but was unable to leverage a favourable political setting. However, changes may occur if the AfD and/or the FDP are able to successfully attack the CDU/CSU in the area of its core competences like economic and tax policy or migration policy.

Economic forecasts

	Real GDP (% growth)			Consumer Prices* (% growth)			Current Account (% of GDP)			Fiscal Balance (% of GDP)		
	2014F	2015F	2016F	2014F	2015F	2016F	2014F	2015F	2016F	2014F	2015F	2016F
Euroland	0.9	1.4	1.6	0.4	-0.3	1.2	2.4	2.2	2.0	-2.6	-2.5	-2.3
Germany	1.6	2.0	1.7	0.9	0.0	1.5	7.4	8.4	8.2	0.6	0.6	0.7
France	0.4	1.1	1.6	0.6	-0.1	1.1	-1.8	-1.8	-1.5	-4.4	-4.2	-3.9
Italy	-0.4	0.5	1.3	0.2	-0.2	1.0	1.8	2.4	2.2	-3.0	-2.7	-2.7
Spain	1.4	2.4	2.3	-0.2	-1.0	1.5	0.4	1.8	1.8	-5.4	-4.3	-3.4
Netherlands	0.8	1.7	1.1	0.3	0.1	1.4	10.9	11.4	11.5	-2.5	-2.0	-1.9
Belgium	1.0	1.3	1.6	0.5	0.2	1.5	1.0	1.5	1.0	-2.8	-2.8	-2.5
Austria	0.3	1.2	1.8	1.5	0.8	1.7	0.7	1.2	1.5	-2.3	-1.6	-1.2
Finland	0.0	0.9	1.4	1.2	0.6	1.3	-1.2	-1.2	-0.9	-2.6	-2.2	-1.6
Greece	0.8	2.5	3.0	-1.4	-1.8	1.0	0.5	1.5	2.0	-1.3	0.5	1.9
Portugal	0.9	1.4	1.6	-0.2	0.1	1.3	0.5	0.8	1.0	-4.7	-3.5	-3.3
Ireland	4.5	3.7	3.5	0.3	-0.1	1.7	4.5	5.5	6.0	-3.6	-2.9	-2.8
UK	2.6	2.5	2.3	1.5	0.9	1.7	-5.0	-4.0	-3.5	-4.9	-3.9	-2.0
Denmark	0.9	1.7	1.8	0.6	1.0	1.5	6.8	6.5	6.0	-1.0	-2.5	-2.0
Norway	2.2	2.4	2.5	2.0	2.0	2.0	10.5	10.0	9.5	10.0	9.5	9.0
Sweden	1.9	2.3	2.8	-0.2	0.5	1.5	5.9	5.3	4.8	-2.0	-1.5	-1.0
Switzerland	1.7	1.8	2.0	0.0	0.4	0.8	11.0	10.8	10.5	0.0	0.4	0.8
Czech Republic	2.4	2.5	2.7	0.4	0.3	1.9	-1.0	-0.8	-0.6	-1.3	-2.1	-2.2
Hungary	3.4	2.4	2.3	-0.2	-0.5	2.8	3.8	3.8	3.7	-2.9	-2.7	-2.4
Poland	3.3	3.3	3.5	0.0	0.3	1.5	-2.6	-2.9	-3.1	-3.4	-2.9	-2.7
United States	2.4	3.4	3.1	1.6	0.6	2.7	-2.6	-2.9	-3.2	-2.9	-2.6	-2.9
Japan	0.0	0.7	1.8	2.7	0.9	0.9	0.6	3.4	3.3	-5.9	-5.2	-4.3
China	7.4	7.0	6.7	2.0	1.8	2.7	3.1	3.4	3.3	-2.1	-3.0	-3.0
World	3.4	3.4	3.8	3.7	3.2	3.8						

*Consumer price data for European countries based on harmonized price indices except for Germany. This can lead to discrepancies compared to other DB publications.
Sources: National Authorities, Deutsche Bank

Forecasts: German GDP growth by components, % qoq, annual data % yoy

						2014				2015			
	2012	2013	2014	2015F	2016F	Q1	Q2	Q3	Q4	Q1F	Q2F	Q3F	Q4F
Real GDP	0.4	0.1	1.6	2.0	1.7	0.8	-0.1	0.1	0.7	0.5	0.4	0.4	0.3
Private consumption	0.7	0.8	1.2	2.1	0.9	0.6	0.0	0.8	0.8	0.5	0.4	0.4	0.3
Gov't expenditure	1.2	0.7	1.1	1.0	0.4	0.1	0.6	0.6	0.2	0.1	0.2	0.3	0.2
Fixed investment	-0.7	-0.6	3.4	2.5	2.3	3.0	-1.7	-1.2	1.2	0.9	0.5	1.0	0.6
Investment in M&E	-3.1	-2.4	4.3	3.8	3.8	2.0	0.6	-1.4	0.4	1.2	0.9	2.0	1.0
Construction	0.6	-0.1	3.6	2.7	2.1	4.5	-3.7	-1.5	2.1	1.0	0.4	0.7	0.6
Inventories, pp	-1.4	0.2	-0.4	-0.3	0.1	-0.1	0.1	-0.5	-0.2	0.0	0.1	0.1	0.0
Exports	2.8	1.6	3.9	5.1	5.0	-0.4	1.0	2.0	1.3	0.7	0.9	1.0	1.2
Imports	0.0	3.1	3.4	5.0	4.5	-0.3	1.2	1.3	1.0	0.7	1.2	1.5	1.5
Net exports, pp	1.3	-0.5	0.4	0.4	0.6	-0.1	0.0	0.4	0.2	0.1	-0.1	-0.1	-0.1
Consumer prices*	2.0	1.5	0.9	0.0	1.5	1.2	1.1	0.8	0.5	-0.3	-0.1	0.1	0.5
Unemployment rate, %	6.8	6.9	6.7	6.5	6.6	6.8	6.7	6.7	6.6	6.5	6.5	6.5	6.6
Industrial production	-0.4	0.1	1.4	1.7	2.0								
Budget balance, % GDP	0.1	0.0	0.6	0.6	0.7								
Public debt, % GDP	81.0	78.4	73.3	69.3	65.8								
Balance on current account, % GDP	7.1	6.7	7.4	8.4	8.2								
Balance on current account, EUR bn	196	189	215	253	257								

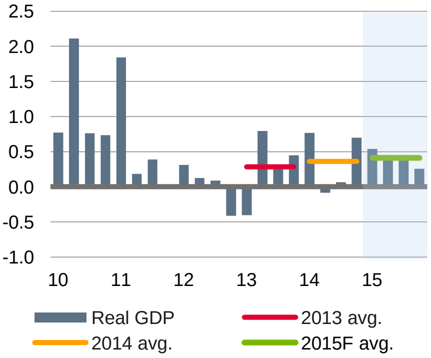
*Inflation data for Germany based on national definition. This can lead to discrepancies to other DB publications.
Sources: Federal Statistical Office, German Bundesbank, Federal Employment Agency, Deutsche Bank Research

Germany: Taking the leap of faith; raising 2015F GDP growth to 2%

- The Q4 GDP details corroborate that the German economy ended 2014 on a high note (+0.7% qoq vs +0.1% qoq prev.) as private consumption received a substantial stimulus from the drop of the oil price (+0.8% qoq vs +0.8% qoq). Investment was up, too, partly thanks to the mild weather, but it lacks underlying momentum given low capacity utilization. Export growth continued to recover, but so far remains well below pre-crisis trends. Still, even net exports added to Q4 growth.
- Updated fiscal numbers show that the general government sector achieved an even higher surplus of 0.6% of GDP in 2014 after 0.1% in 2013 and 2012. All government levels showed a surplus with more than half of the surplus coming from the federal level.
- We increase our 2015 GDP forecast to 2.0% from 1.4% previously. This is especially due to the much larger carry-over effect (0.5%-points compared to 0.2 before) courtesy of the marked Q4 GDP growth. In addition, we raise our Q1 GDP forecast from 0.3% qoq to 0.5% qoq as the renewed oil price drop will boost consumption again (quarter to date in Q1: -25% qoq in EUR compared to -20% in Q4). Sentiment also improved further in January/February with ifo expectations and the composite PMI pointing to 0.5% and 0.4% growth, respectively. Growth should gradually slow thereafter as the oil price stimulus declines, and potentially partly reverses, and the negative effects from the minimum wage show up. At the same time, the material falls in the EUR should gradually support exports later in the year providing some support for investment.

Strong growth in Q4 2014 1

Real GDP, % qoq



Sources: Federal Statistical Office, Deutsche Bank Research

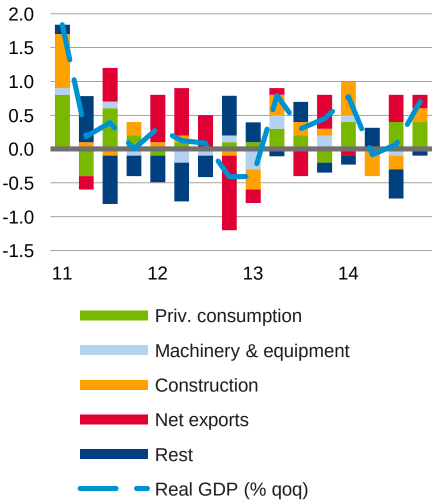
Q4 GDP: Consumption boom thanks to oil price decline

The Q4 GDP details corroborate that the German economy ended 2014 on a high note. Real GPD grew by 0.7% qoq after stagnating in the previous two quarters (Q2: -0.1%; Q3: +0.1%). This left GDP up 1.6% yoy in the fourth quarter as well as in 2014 as a whole. Headline GDP growth of previous quarters was not revised, while there were some moderate revisions to the components. The Q4 growth rate was much higher than the initial assessment of the Federal Statistical Office (+1/4 % qoq) that it had voiced during the press conference on 2014 GDP in January.

As expected Q4 growth was tilted strongly towards domestic demand as private consumption (+0.8% qoq vs +0.8% prev.) showed the strongest two quarters since 2010/11 thanks to a marked boost from the decline in oil prices. The consumption increase equalled a 0.4%-point contribution to overall growth or more than half the total. While the stimulus from the decline of the oil price – 20% qoq in Q4 in EUR – to real disposable income certainly was the major reason, the income side was also supported by other factors. Employment continued to grow (+0.2% qoq), while e.g. negotiated wages were up 2.7% yoy. This is in line with employee compensation still being the major driver of overall income growth (+3.6% yoy), but even property and entrepreneurial income picked up (+1.7% yoy) after roughly stagnating in the previous three quarters. Still, the savings rate increased markedly to 9.8% after roughly averaging 9.2% in the previous 9 quarters. This suggests that part of the windfall gains have surprised households and might lead to higher spending in the following quarters.

Private consumption boosted Q4 GDP 2

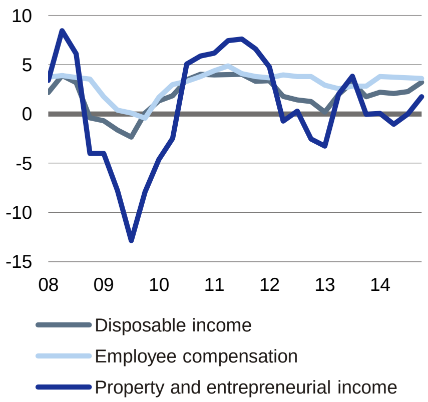
Contribution to real GDP growth, qoq, %-points



Sources: Federal Statistical Office, Deutsche Bank Research

Property and entrepreneurial income picks up 3

% yoy, nominal



Source: Federal Statistical Office

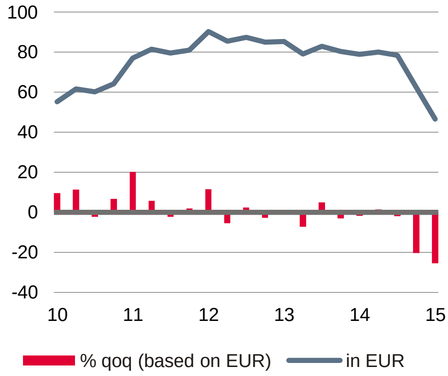
Jump in saving rate 4

%, sa

Source: Federal Statistical Office

Oil price drop also in Q1 2015 5

Oil price, Brent, in EUR, quarter-to-date avg.

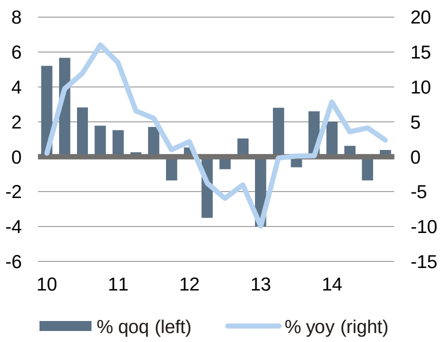


Sources: Deutsche Bank Research, IHS

Investment was a moderate positive adding 0.2% points to overall growth. However, this was largely due to construction (+2.1% qoq) that benefitted from mild weather after investment declined in the two previous quarters. Monthly construction data as well as the construction ifo disappointed lately as the construction ifo declined modestly several months in a row, while permit growth slowed markedly from over 10% yoy to around 5% yoy towards the end of 2014. Even equipment investment rose in Q4 despite the weakness of orders, but the rate was modest (+0.4%) especially compared with the previous quarter's decline (-1.4%). With capacity utilization only rising above its historic average in Q1 2015, moderate order growth and geopolitical risks, companies remained reluctant to add much to their capital stock.

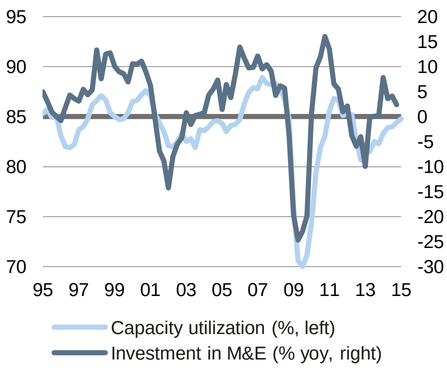
Investment in machinery & equipment: Modest pace 6

% qoq (left), % yoy (right)



Source: Federal Statistical Office

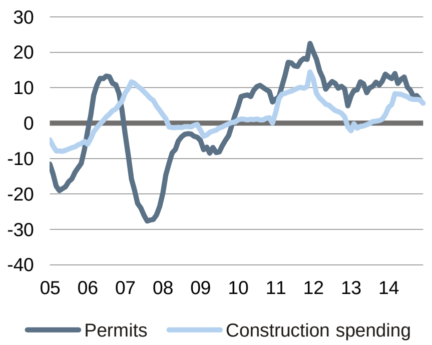
Capacity utilization not pointing to strong investment growth 7



Sources: EU Commission, Federal Statistical Office

Construction permits have slowed 8

% yoy, 12M mov. avg.



Source: Federal Statistical Office

Foreign trade was a positive, but lacks momentum compared to pre-crisis years. Thanks to the third consecutive solid increase of exports (+1.3% qoq vs +2.0% prev.) and in comparison less dynamic import growth (+1.0% vs +1.3% prev.) net exports added 0.2%-points to overall growth in Q4 and 0.4%-points in Q3. While German exports to Russia continued to dampen the overall dynamic other regions were broadly supportive, though, even there is still a lack of underlying momentum. Exports were up nearly 5% yoy in Q3 and Q4 well below double-digit rates enjoyed between 2004 and 2008, which is also reflected in cautious equipment investment spending.

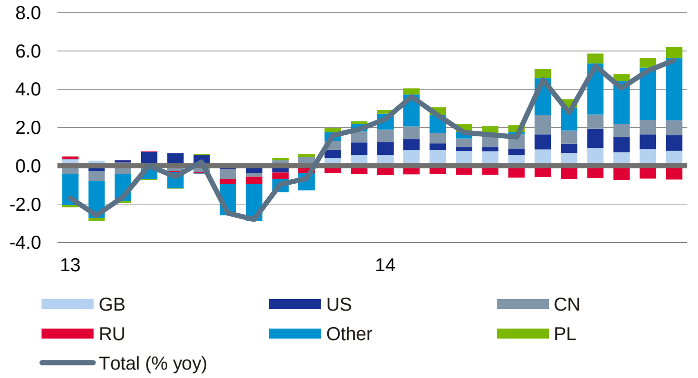
Exports: Moderate recovery path 9

National accounts data, real, % yoy, nsa

Source: Federal Statistical Office

Russia continues to weigh 10

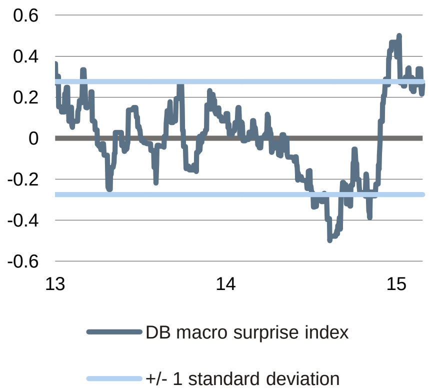
Growth contribution, %-points, 3M mov. avg.



Sources: Federal Statistical Office, Deutsche Bank Research

DB macro surprise index markedly positive 11

Average of last 20 z-scores of data surprises



Values above (below) 0 indicate the data came in better (worse) than expected

Sources: Bloomberg Finance LP, Deutsche Bank Research

2015 GDP: Taking the leap of faith raising our forecast to 2%

We have often put great emphasis on the fact that our GDP forecasts tended to be at the lower end of expectations over the last years. This was driven by our conviction that the export-dependent German economy cannot decouple from weak global trade and the effects of the Euro crisis.

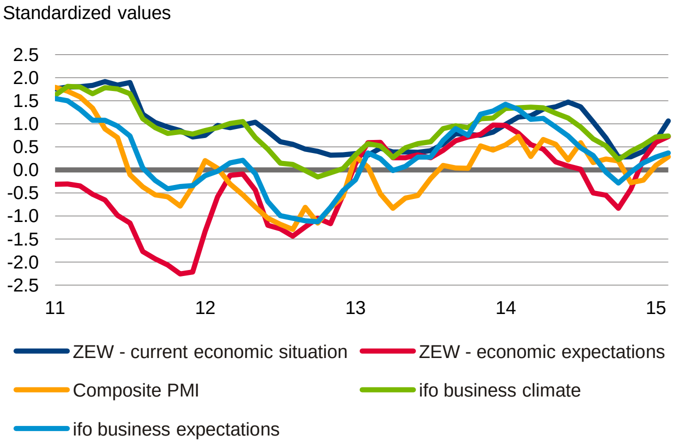
However, with the strong growth observed in Q4 2014, the good start to 2015 according to sentiment data and supported by further declines of the oil price as well as the somewhat brightening outlook for the global economy, in particular for EMU, we raise our forecast for 2015 to 2.0% from 1.4%. This is much higher than the February consensus of 1.5% (Q4 GDP was not available at that time so this should trend up, too).

Growth in 2015 will come primarily from consumption, which we expect to exceed 2% (2.1% qoq vs 1.2% prev.) for only the third time in 15 years (2000 and 2011). Early in the year this will be supposrted by the oil price slump as well as continued strength of the labour market. Wages should show solid underlying momentum (see next section) and receive a one-off boost from the introduction of the minimum wage in January.

Investment spending should moderate somewhat in 2015. Equipment spending should pick up over the course of the year (+3.8% vs +4.3% prev.) thanks in part to EUR weakness that will benefit exports. In contrast, construction is likely to slow (+2.7% vs +3.6%) as indicated by the recent loss of momentum in monthly indicators. Any kind of public infrastructure programme is unlikely to give much impetus to 2015.

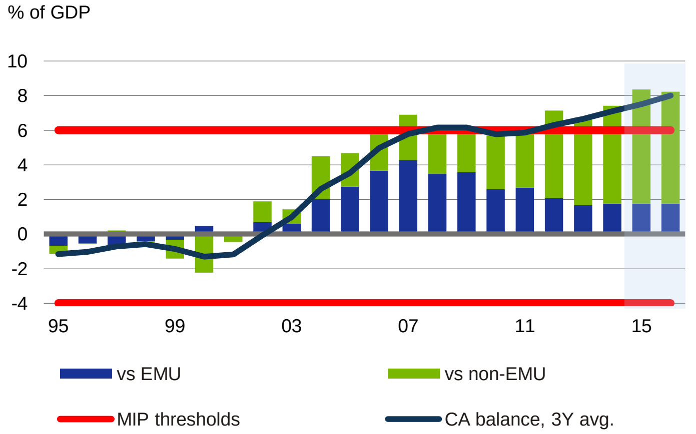
Exports (+5.1% vs +3.9%) and imports (+5.0% vs +3.4%) should both pick up. Given the relatively larger size of exports this will bring the current account surplus to 8.4% compared to 7.4% of GDP in 2014 (oil prices also help). This is (again) a new high and much larger than the upper bound that would be in line with the EU Commission’s macroeconomic imbalances procedure (6%), though, it should be largely due to gains vs non-EMU countries. Still, this will result in further calls on Germany to stimulate its domestic demand.

Marked pick up in sentiment 12



Sources: Markit, ifo, ZEW, Deutsche Bank Research

Current account surplus vs EMU down markedly 13



Sources: Deutsche Bundesbank, Federal Statistical Office, Deutsche Bank Research

This is also true for the fiscal side. While we suspect that the spending spree (e.g. pension package) will weigh on the structural fiscal position, even higher growth should compensate and keep the general budget balance at 0.6% of GDP in 2015. We also lower our CPI forecast (national definition) from +0.1% to 0%.

Germany's surplus for 2014 upward revised to +0.6% of GDP (prev. 0.4%) 14

	2009	2010	2011	2012	2013	2014
General govt. (% of GDP)	-3,0	-4,1	-0,9	0,1	0,1	0,6
General govt. (EUR bn)	-74,5	-104,8	-23,3	2,6	4,2	18,0
Central government	-38,0	-82,2	-27,1	-14,7	-4,5	11,4
State government	-19,3	-20,4	-13,0	-5,7	-2,8	1,9
Local government	-2,7	-6,2	1,4	4,7	5,3	1,3
Social security funds	-14,5	3,9	15,4	18,3	6,1	3,4

Source: Federal Statistical Office

Risks remain high. While some of the tensions surrounding the Greece-negotiations have abated, the complicated nature of the needed compromise will keep risks high over the next months. In addition, the current situation in Ukraine/Russia does not look any less challenging despite the recent brokered peace-cease-fire deal. These factors could limit the pick-up of investment spending. A faster than forecast recovery of the oil price could quickly reverse the positive impact on real disposable income. Global growth estimated to improve slightly in 2015 overshadows the fact that growth in the EM/BRIC states will slow. These have been important destinations for German exports. Russian GDP is expected to decline by 5% in 2015. Also, Chinese growth is set to slow to 7% and our Chinese economist even sees the risk of a mini-hard-landing.

GDP growth should slow to 1.7% in 2016 as the structural headwinds to growth (e.g. lack of domestic reforms and demographics) take their toll. We estimate potential GDP growth to be below 1.5% currently and to slow in the coming years.

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Minimum wage boosts compensation in 2015

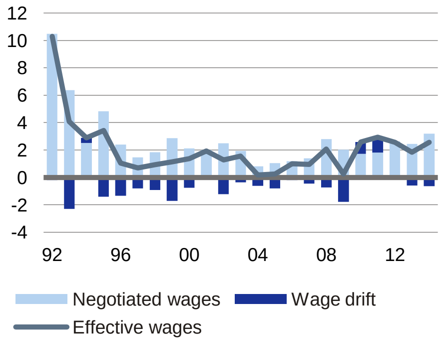
— In 2014, negotiated wages showed the highest growth in 20 years at 3%. Only a few sectors have reported below-average wage growth of late.

— Given the unusually positive labour market situation and the very robust outlook, negotiated wages are poised to increase by roughly 3% again in 2015. With their close to 4 million employees and agreement of a 3.4% pay rise in early 2015, the metal and electrical engineering sectors are likely to have set the benchmark. Most of the demands made to date call for wage hikes of over 5%.

— While the minimum wage could limit the room for manoeuvre in the middle to upper wage brackets in the short term, it will probably tend to exert upward pressure on negotiated wages in the medium term. Moreover, it will give the overall wage level a one-off boost. German unit labour costs are likely to increase noticeably in 2015.

2014: Wage growth with 20-year-high 1

Total economy, % yoy



Sources: Federal Statistical Office, Deutsche Bank Research, Deutsche Bundesbank

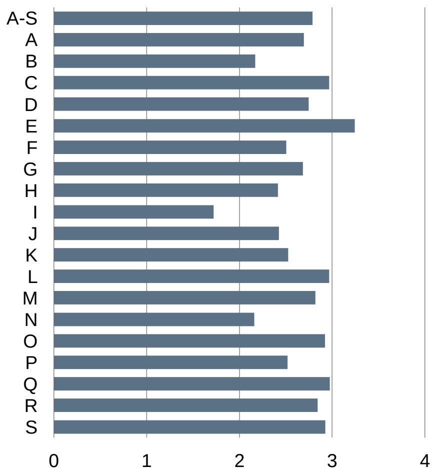
2014: Wage growth at 20-year high

In 2014, Germany's employees saw a 3%[1] increase in negotiated wages (monthly basis), enjoying the highest collectively bargained wage growth since 1993. Even taking account of the fact that effective wages rose at a slightly slower pace (+2.6%) since, for example, bonus payments were rather meagre (negative wage drift) due to economic uncertainties, this is nonetheless the second-highest growth since 1994. This is the result of the unusually good conditions in Germany's labour market: unemployment is at a record low and falling; employment and the number of job vacancies are at record highs and climbing.

All in all, the positive negotiated wage growth was broadly based. Taking the average growth in negotiated wages over the past two years, there are only four significant deviations from the 2.6% average – in hotels and catering, mining, energy sector and other business-related services the increase fell more than 0.4 of a percentage point (pp) short of the overall average.

Only few outliers at sector level* 2

Negotiated wages, incl. one-off payments, monthly basis, % yoy, average 2013-2014



* According to NACE codes

Source: Federal Statistical Office

The high 2014 average was noticeably shaped by the dynamic growth at the start of the year, though. Until June 2014 the growth accelerated to over 3.5% yoy – such rates had not been seen since early 2008. In the second half of the year the growth rates receded to roughly 2.8%, but this roughly corresponds to the level in the past few years. Apart from a base effect there are probably two main reasons for this: at mid-year the German economy and its growth prospects had clouded over noticeably owing to geopolitical risks and one-off effects, which are thought to have strengthened the employers' bargaining position. Moreover, the two-stage wage agreements agreed in the previous year also had a damping effect as the second stage in the following year usually provided for a smaller increase.[2]

Slowdown in H2 2014 3

Negotiated wages, monthly basis, excl. one-offs and ancillary payments, % yoy

Source: Deutsche Bundesbank

Negotiated wages in 2015: Outlook remains bright

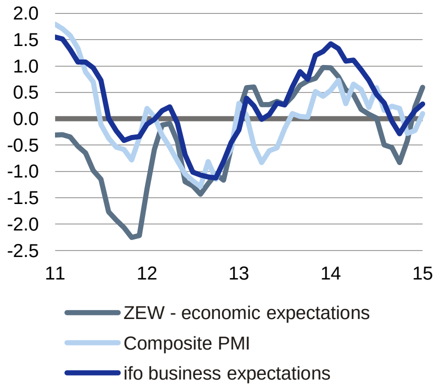
All things considered, wage prospects continue to look good – from an employee standpoint. We assume that German GDP will expand by 2.0% in 2015 and thus faster than in 2014 (1.6%). The growth of employment ought to continue at a slightly more moderate pace and unemployment should decline

[1] Data from Deutsche Bundesbank. The Federal Statistical Office even published a rate of 3.2%.
[2] We had pointed this out in our last report on wage growth. However, we had slightly under-estimated the wage dynamics as a whole. See: So far, so good. Focus Germany. May 2, 2014.

further. Productivity is set to improve more noticeably in 2015 than back in 2014 (0.2% then as opposed to 1.1% now) thanks to increasing (but all in all still moderate) capacity utilisation. Leading indicators for the labour market (ifo employment barometer, IAB labour market barometer) have brightened again of late. These arguments will probably underpin the trade unions' bargaining position and help to ensure that the wage negotiations continue to reach average settlements of significantly more than 2%.

Sentiment has turned 4

Standardised values



Sources: Markit, ifo, ZEW, Deutsche Bank Research

The employers' arguments against "excessively high" wage agreements will probably include the still major geopolitical risks (Ukraine, Russia), EMU-specific uncertainties (Greece), sharply declining inflation rates, competitive gains of foreign rivals and the strongly rising wage costs in some sectors triggered by the minimum wage. However, these arguments are only partly valid. For instance, the risks to the outlook are too diffuse to be able to play a significant role. In particular, business surveys (ifo, PMI) show that company leaders have become much more optimistic. Given our expectation of an inflation rate of 0.0% the nominal wage increase would translate unchanged into real wage growth. However, the negotiations tend to be geared to core inflation, which remained pretty stable in 2014 at just over 1%, as in 2013.

Minimum wage to have contradictory effects

The minimum wage will have varied yet unclear effects on negotiated wage growth in 2015. The direct effects are limited since the minimum wage is a statutory arrangement and thus it is not factored into negotiated wage growth. However, the negotiating parties in several sectors affected by the minimum wage (about one million employees altogether) have agreed transitional arrangements which do indeed provide for noticeable wage hikes but initially remain shy of the minimum wage. These are also included in the negotiated wage growth analysed here and they induce upward pressure.

The indirect effects are potentially larger, but they are also more difficult to quantify. On the one hand, the minimum wage causes tangible cost pressure, although the current state of the economy will presumably provide the companies with pretty good chances of passing on a relatively large part of the costs to the consumer. Nonetheless, this will probably limit the room for manoeuvre for employees in higher wage brackets. In our opinion, this argument is likely to carry the heaviest weight in 2015. On the other hand, especially those employees who up to now have earned only slightly more than the minimum wage will push to ensure that the wage differential is maintained. This was already to be observed in the last settlement for the civil service (partly an absolute pay rise instead of a percentage increase) and could increasingly lead to wage pressures over the coming years.

Metal industry ushers in wage round

New collective wage contracts will be negotiated in 2015 for roughly 11 million employees – over 25% of the total workforce. The metal and electrical engineering sectors with their well in excess of three million employees are the highlight, especially since they are seen as setting a (kind of) benchmark for negotiations not only in the manufacturing industry. These talks have been underway since the start of 2015. On February 24 the negotiating partners agreed a hefty wage hike of 3.4% (from April 2015) as well as a one-off payment of EUR 150. The agreement runs until March 2016. Combined with the effects of the increase last year, metal sector wages are set to rise by 3.6% on average in 2015. Originally the union had called for a 5.5% increase and the employers first offered 2.2%.

The chemicals industry (over 500,000 workers) and the civil service at the federal state (Länder) level (over 800,000) are also in the midst of significant bargaining rounds that may be concluded before the end of the first half. Negotiations in the retail sector (with a total of over 1.5 million employees) are set to begin towards mid-2015, to be followed by the wholesale and foreign trade sector (over 700,000).

Most of the demands made public to date call for a 5.5% wage increase, with the chemicals industry marking the lower end of the range at 4.8%. In some sectors the demands also contain "qualitative" features, such as early-retirement schemes or transitional pension arrangements. These can likewise entail noticeable costs for companies.

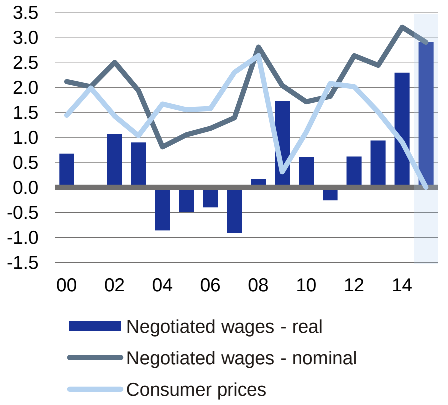
Wage negotiations in selected* sectors 5

Sector	Expiry date	Wage demands	Result	Employees
Metals and electrical engineering (west and east)	Dec 31, 2014	5.5%: 12 months	+3.4%; lump-sum payment of EUR 150; 15 month run time (March 2016)	3.480.200
Civil service (federal states, west and east, excl. Berlin)		5.5%, at least EUR 175 per month, 12 months		822.500
Hotels and catering		5.5%: 12 months		199.700
Chemicals (North Rhine, Hesse, Rhineland-Palatinate)	February 28, 2015	4.8%: 12 months		230.900
Volkswagen AG		5.5%: 12 months		110.000
Retail (Hesse, Saarland, Baden-Wuerttemberg)	March 31, 2015			472.200
Wholesale and foreign trade (Baden-Wuerttemberg, Bavaria, Saxony)				395.700
Chemicals (Schleswig-Holstein, Hamburg, Lower Saxony, Bremen, Westphalia, Baden-Wuerttemberg, Bavaria, west Berlin)		4.8%: 12 months		261.800
Insurance (east and west)		5.5%, at least EUR 160, 12 months		173.700
Retail (Schleswig-Holstein, Hamburg, Lower Saxony, Bremen, North Rhine-Westphalia, Rhineland-Palatinate, Bavaria)	April 30, 2015			1.291.800
Wholesale and foreign trade (Schleswig-Holstein, Hamburg, Lower Saxony/ Bremen, North Rhine-Westphalia, Hesse, Rhineland-Rhine Hesse, Palatinate, Berlin, Brandenburg, Mecklenburg-Western Pomerania, Saxony-Anhalt, Thuringia)				720.300
Motor vehicle sales and servicing (Lower Saxony, Hesse, Rhineland-Rhine Hesse, Palatinate, Saarland, Baden-Wuerttemberg, Bavaria, Berlin/Brandenburg, Saxony-Anhalt, Thuringia, Saxony)				267.000
Retail (Saxony-Anhalt, Thuringia, Saxony)	May 31, 2015			195.500
Deutsche Post AG				132.000
Retail (Berlin, Mecklenburg-Western Pomerania, Brandenburg)	June 30, 2015			189.400
Agriculture (west and east excl. Lower Saxony, Mecklenburg-Western Pomerania)				134.000
Industrial cleaners (west and east)	October 31, 2015			396.100
Wood and plastics processing (Lower Saxony/Bremen, Westphalia-Lippe, Hesse, Rhineland-Palatinate, Baden-Wuerttemberg, Bavaria, Saxony-Anhalt, Thuringia, Saxony)	December 31, 2015			176.700

*Negotiations for more than 100,000 employees
Sources: WSI-Tarifachiv, Deutsche Bank Research

2015: Huge real wage increase 6

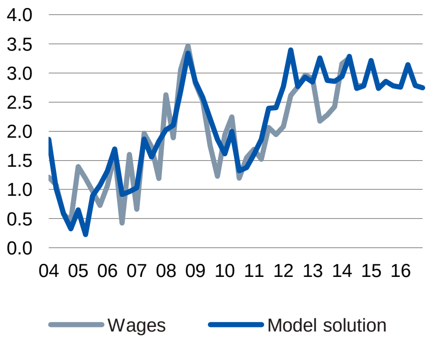
% yoy



Sources: Federal Statistical Office, Deutsche Bank Deutsche Bundesbank

Negotiated wages: Forecast model suggests strong growth also for 2015 7

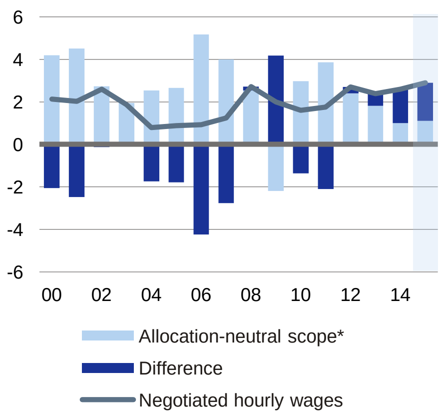
% yoy



Sources: Bundesbank, Destatis, Deutsche Bank Research

Allocation-neutral scope: Probably over-exhausted again in 2015 8

Hourly basis, nominal, % yoy



* Inflation rate + productivity growth

Sources: Federal Statistical Office, Deutsche Bank Research

Negotiated wages could rise by close to 3%

According to a rule of thumb the trade unions' wage demands are met at roughly the half-way point, and the deviation from the mean is determined by the negotiating clout of the respective employee/employer representatives. Since we currently see the employee side having an advantage, the settlements will probably tend to be closer to 3% and thus roughly the same as last year. As the economic environment had darkened in mid/end-2014, we had still been expecting a moderate slowing of the wage dynamics.

This qualitative assessment fits well with the results of a simple yet reliable statistical model. This model factors in the productivity and core inflation readings of the previous quarters with a time lag. These mainly stand for costs and revenues on the companies' side. Moreover, the current unemployment rate is also factored in, reflecting the relative clout of the negotiating parties. Since unemployment is likely to fall slightly but productivity declined in the past year and core inflation was stable, the model points, as in the previous year, to 2.9% higher wages. The employees' robust negotiating position points to upward risks, while the two-stage settlements agreed last year will probably again help to vent the pressure. We therefore forecast that nominal negotiated wages will increase by 2.9%. With inflation non-existent at 0.0% this would leave a marked increase in real wages of 2.9% – the highest value since 1995.

Allocation-neutral scope exceeded by far

The allocation-neutral scope of negotiations is likely to be exceeded by far in 2015. This concept is usually applied to assess how much scope is provided for wage increments by economic growth without the employees/employers falling into a poorer or better position in relative terms. In this context, the sum of productivity growth (cost-cutting) and the inflation rate (selling prices) is determined and set against wage growth. Given our inflation rate forecast of 0.0% and moderate productivity growth of 1.1% in juxtaposition with a renewed surge in wages of roughly 3% the scope is likely to be exceeded by far for the third year in a row. However, the pronounced decline in the inflation rate that has been driven by falling energy prices is not as likely to lead to lower selling prices for companies but rather will tend to produce cost savings on the input side. But even if this is taken into account, income distribution – as in past years – will continue to shift more towards the employee side.

This effect will be noticeably compounded by the minimum wage. In fact, effective wages are poised for even more vigorous growth in 2015 than are negotiated wages. The minimum wage being paid to about 3.7 million employees not covered by a negotiated agreement will cause a one-off additional push which could be tantamount to positive wage drift of 1.5 pp.[3] This would thus lift wage income (monthly basis) by considerably more than 4%. All of these factors would probably play a part in boosting German unit labour costs substantially (+3.3%) in 2015.

Oliver Rakau (+49 69 910-31875, oliver.rakau@db.com)

[3] See: Strong domestic economy to suffer from good intentions. Focus Germany. June 3, 2014.

Is the ECB spoiling the Germans' appetite for saving?

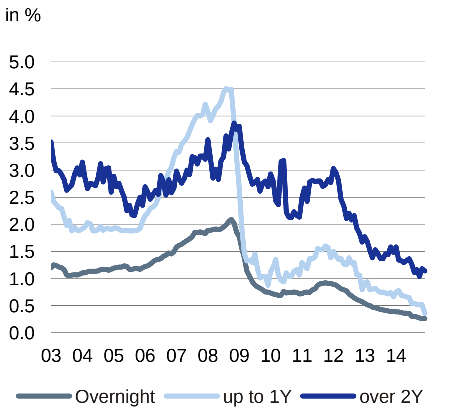
— Deposit rates in Germany have fallen below 0.5%, Bund yields are negative for maturities of up to 6 years. Nevertheless, Germany's savings ratio appears to have hardly reacted to this.

— Although the net savings ratio has fallen slightly in recent years, this is mainly the result of higher writedowns on the real estate assets of households as a consequence of rising construction investment and prices. Also, the savings ratio stabilised in the course of 2014. In the final quarter there were unexpected, oil price-induced real income gains which even resulted in a strong increase of the savings ratio.

— The standard theories on household saving make contradictory assertions about the role of interest rates. Surveys and our simple econometric model to explain saving show that interest rates do not have a significant influence on savings decisions. It does not even appear to be a major factor in investment decision-making by German households.

— All the same, the savings ratio is expected to decline over the next few years. This is initially because of the effect of continually rising construction investment and prices. In the medium term, however, the dissaving of the retired baby boomers will be the decisive factor in the continued decline in the savings ratio.

Interest rates on housholds' deposits (new business) 1



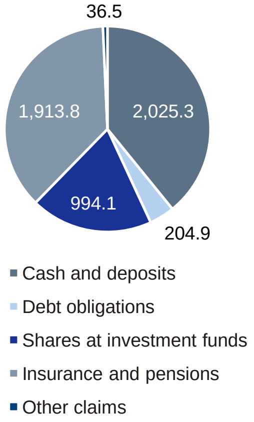
Source: Deutsche Bundesbank

In the meantime the interest rates for short-term deposits by households at German banks have dropped to below 0.5%. Bund yields on maturities up to 6 years are negative. The German government has to pay a coupon of just 0.4% on 10-year bonds. Under headlines such as “dire straits for investing” or “it no longer pays to save”, a debate has been underway in Germany for some time already about whether the ECB's monetary policy prompts German households – despite their high propensity to save by international standards – to consume a larger proportion of their income or even to increase their debt levels again. In some locations outside Germany and at international institutions such as the IMF or the OECD, by contrast, vehement demands are being made for a reduction in Germany's savings ratio to foster stronger consumption growth as Germany's contribution to the reduction of global and intra-European imbalances. The near-record low propensity to save (determined by the monthly consumer confidence surveys) and the drop in the household savings ratio between 2010 and 2013 – which did not continue in 2014 – do not appear to support such expectations.

In the following we start by introducing the standard economic explanatory models of saving behaviour, focusing our attention on the role of the interest rate. Thereby we attempt to understand the development of the German savings ratio in the last few decades and examine additional statistics and surveys of saving behaviour in Germany for signs of changes in savings habits or structural breaks. Since the theories are based on very restrictive assumptions about human behaviour and provide partly contradictory explanations, in the next step we introduce a simple econometric model of savings activity in order to test whether a significant interest rate effect can be established in addition to other factors. Since theories are only in part corroborated by empirical evidence and since our empirical model does not provide a sufficient explanation of the savings behaviour, we then examine to what degree conclusions can be drawn about the potential reactions of households to the extremely low interest rate environment using behavioural economic approaches.

Monetary assets of private households 2

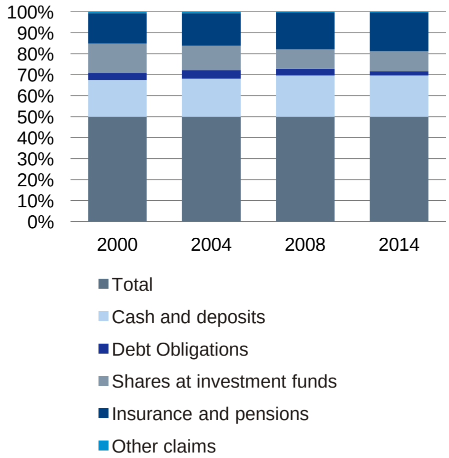
EUR bn



Source: Bundesbank

Financial assets of private households 3

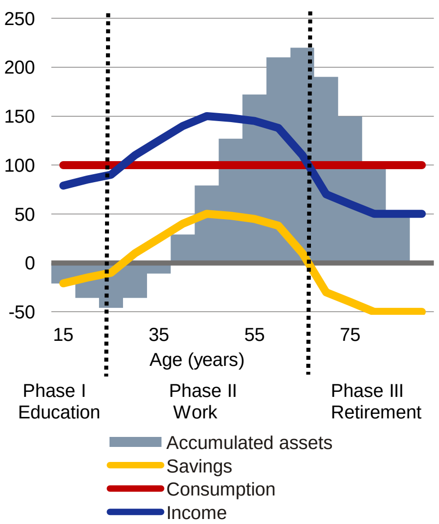
in %



Source: Eurostat

Stylised illustration of life-cycle hypothesis 4

Monetary units



Source: Deutsche Bank Research

Theoretical statements about saving – "it depends"

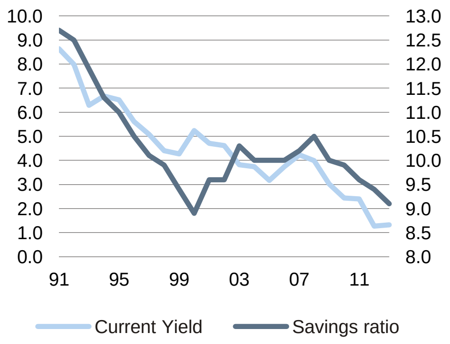
According to the microeconomic theory of the household the formation of savings is dependent on the time preference of households as well as on household income. The time preference rate signifies how households weight current consumption against future consumption. Households in principle prefer current consumption. In order to refrain from current consumption in favour of future consumption, i.e. saving, households demand compensation in the form of an interest payment. The interest rate corresponds with the (aggregate) time preference of households, according to this theory. Household theory states that a reduction in the interest rate leads to a decline in saving. However, depending on the shape of the indifference curves that depict the combinations of current and future consumption at which households are indifferent, an abnormal reaction is also possible in which households increase their saving despite falling interest rates.[4] In addition, besides the price (interest) effect which is also referred to as the substitution effect (between current and future consumption) there are other effects that need to be taken into consideration. Depending on a household's net asset position – in Germany households have total net financial assets of EUR 3,625.5 bn (Q1 2014) that are mainly held in the form of cash and deposits and claims on insurance policies – interest rate changes influence the household's current and possibly also future interest income (income effects). Moreover, interest rate changes can also influence the prices of other asset classes, such as shares or also real estate, even though these effects in Germany are relatively minor not least because of the country's low level of share ownership and low homeownership ratio[5]. Still, it should thus be clear that no definitive statements about the overall effect can be derived from the household theory. This applies to the individual household with its subjective time preference, age structure, asset position and risk preference, but also for the entire household sector within the economy.

The permanent income [6]and life cycle hypotheses[7] are dynamic observation approaches. These are based on the Keynesian view that consumption is mainly determined by current household income. However, they postulate that households try to stabilise their consumption at a certain level on the basis of their expected future income and asset development over their entire life cycle. Assuming unimpeded access to credit, the savings ratio then follows income development. In a person's first decades savings are negative; education and homebuilding are financed via credit. Then as income rises debt is reduced and assets are accumulated. After completion of the employment phase this is then used up (dissaving) in order to maintain one's level of consumption. In this model the interest rate is not a major factor. However, age-specific savings ratios for Germany computed by the income and consumption sample survey or the Socio-economic Panel (DIW) only partially conform with the pattern set by the life cycle model. In particular after ending the gainful employment phase households at best see a decline in their savings ratio, but no dissaving. In its October 2011 monthly report the Bundesbank found that "pensioners are not dissaving in the expected manner".[8] The reason for this is the strong intertemporal income shift due to the German pensions system, from which German pensioner households currently still receive around 3/4 of their income. Pension insurance contributions are deducted from gross income and are thus not included in savings (net income – consumption expenditure). Of course the model's assumptions, especially perfect foresight, which evidently also

[4] Woll, Allgemeine Volkswirtschaftstheorie, 7th edition.
[5] OECD Economic Studies No. 35, 2002/02.
[6] Friedman M. (1975). A theory of the consumption function".
[7] Ando A., Modigliani F. (1963). The 'life cycle' hypothesis of Saving: Aggregate Implications and Tests.
[8] Deutsche Bundesbank (2011). Monthly Report October 2011.

Relation of interest yields and saving behavior (annual) 5

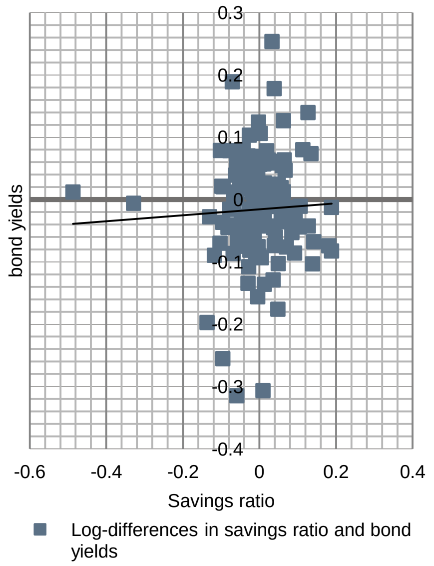
Current Yield (llhs) und savings ratio (rhs)
in %



Source: Federal Statistical Office Germany

Low correlation in log differences 6

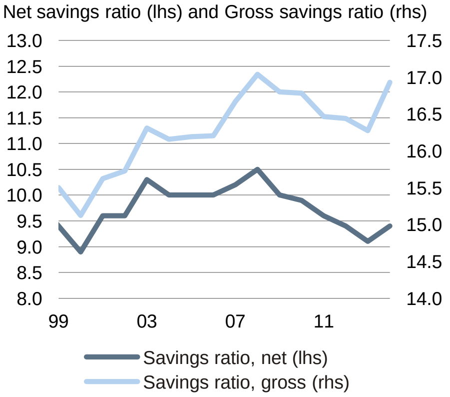
Log-differences



Source: Federal Statistical Office Germany, Deutsche Bank Research

The contrast in net / gross savings ratio 7

Net savings ratio (lhs) and Gross savings ratio (rhs)



Source: Federal Statistical Office Germany

presupposes knowledge of the time of one's death in order to determine the necessary expenditure flows, do not correspond with reality. Also, the saving is additionally influenced by other motives such as the desire to bequeath or by the increasingly important risk of a longevity given the rising cost of nursing care and the declining level of guaranteed state benefits.

Especially changes that reduce the benefits that can be expected from the state pension scheme for the future generation of pensioners should – as long as there is not a corresponding increase in the expected length of the working life at the same time – lead to households making greater efforts to save. According a recent survey, 2/3 of respondents fear that their state pension will not be sufficient to live on. Such changes of a more structural nature, which of course include the demographic shift, can scarcely be separated from cyclical factors such as income or interest rates in the analysis. Chart 5 suggests a close correlation between the savings rate and the interest-rate level. This is probably the result of more fundamental macroeconomic trends affecting both variables at certain times. But if one looks at the changes of both time series (Chart 6) it becomes evident that there is only limited correlation. The interest-rate elasticity of the savings rate is therefore not significantly different from zero, i.e. interest-rate changes in the current or previous period having only marginal impact on the current German savings rate. This may also have something to do with the fact that a large proportion of saving is executed via fixed savings plans in which the decision about the amount was made in advance, as is the case for example with insurance-linked saving or also a building society savings plan. In Germany there are more than 16 million Riester savings plans and about 90 m life insurance policies, whose savings contributions are fixed at least for the short term. However, the historical relationships allow only limited assertions to be made about the expected reaction of German households to the current – all-time – low level of interest rates. It could well be that there is a non-linear reaction of households especially close to the “zero level”. This could be the case for example because of psychological “anchor effects” (see final section).

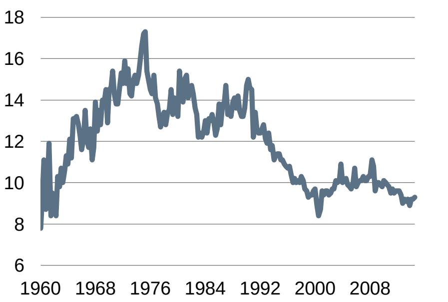
Long-term downtrend in German savings ratio

In the national accounts a figure is usually reported for the household net savings ratio. This is computed by setting current savings plus the changes in occupational pension claims (that are not included in disposable income) against disposable income. Current saving is the difference between current household income and household consumption expenditure. Household income includes, apart from net wages and salaries, monetary social security benefits provided by the state and net transfers as well as profit income. The latter comprises operating surpluses, income from self-employment and asset income. Asset changes, for example resulting from revaluations or disposals, remain unreported in this item, as they impact on stock variables but not the current flow variables. For the net savings ratio the writedowns on property portfolios of households at replacement prices are deducted from profit income. Due to fluctuations in the capital stock and the movements in replacement prices there can be marked differences between the development patterns of net and gross savings ratios. Since writedowns on the housing stock are partly the result of earlier savings accumulation, the gross savings ratio can be a better indicator of household propensity to save – depending on the problem analysed.

The development of the German savings ratio over the last 55 years can roughly be divided into four phases. Firstly there was a steady increase from less than 10% in the early 1960s to more than 17% in H1 1975. Given the partly contradictory theoretical explanations it is difficult to identify the drivers of this development. However, throughout this phase not only nominal but also real

Savings ratio 8

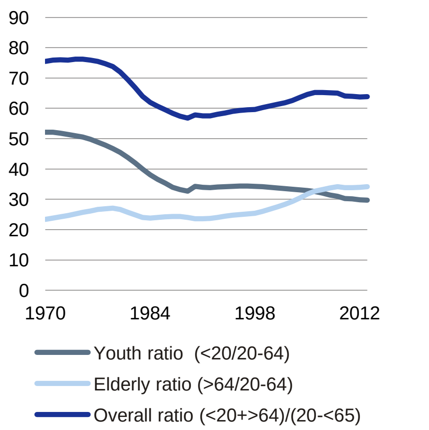
in %



Source: Federal Statistical Office Germany

Age structure (1970-2013) 9

Percentage of working population



Source: Federal Statistical Office Germany

Income inequality and savings ratio 10

Gini-Index (lhs) and Savings ratio (rhs) in %

Source: Federal Statistical Office Germany and Worldbank

interest rates were very high. In 1974 the current yield climbed to over 10% as inflation rose due to the oil price shock. At the same time sovereign debt increased sharply during the first half of the 1970s. The high savings ratio at that time could thus be interpreted as an indicator of Ricardian equivalence. According to the latter, rational households respond to rising sovereign debt by raising their savings ratio as they expect a higher tax burden in the future as a consequence of the increasing level of government debt. In a second phase, which lasted from roughly the mid-1970s until German reunification, the savings ratio hovered within a comparatively narrow band between 12% and 16%. It temporarily peaked in 1981, when the second oil price crisis sent the German inflation rate rising markedly. This may be associated with the so-called Pigou effect (real-balance effect). This forecasts that households react to a pick-up in inflation by boosting their savings ratio, as inflation reduces the real value of nominal cash and asset holdings. Following another high in 1990, which coincided with a reunification-driven increase in the current yield to more than 9%, the savings ratio fell constantly in the following decade and reached a level in summer 2000 of 8.4%, which more or less matched the lows of the early 1970s. During this period came the “great moderation” phase. This describes the phenomenon of globally declining inflation rates and yields. This is partly explained by successful central bank policies, but undoubtedly there were also other factors, such as productivity gains delivered by the globalisation stimulus at that time. In the last twelve years the savings ratio has fluctuated within a very narrow band between 9% and 11%. Since 2011 it has stayed at the lower end of this range.

Demographic shift squeezing aggregate savings ratio

Besides these more “cyclical” factors there are also structural, more long-term factors impacting on the savings ratio. First of all there is the demographic aspect. On account of the marked decline in the birth rate since the 1960s while life expectancy has risen rapidly the age structure of the German population has changed dramatically. In view of budget restrictions savings accumulation over the life cycle occurs at roughly the same time as the individual's gainful employment phase. The ratio of potentially employed cohorts to not yet or no longer employed cohorts should therefore be reflected in the household savings ratio, if cohort sizes differ considerably.

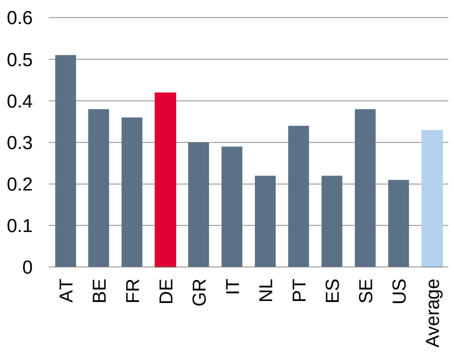
The youth ratio, i.e. the ratio of under-20s to 20-to-60-year-olds has fallen steadily since the start of the 1970s and has currently stabilised at a level of about 30. By contrast, the elderly ratio, i.e. the ratio of over-64s to those aged 20-64 has risen steadily. On balance, the overall dependency ratio (youth plus elderly ratio) has risen by nine points since its low at the end of the 1980s. According to the forecasts by the Federal Statistical Office the overall ratio is set to rise dramatically in the coming years and temporarily flatten out around 2030. The assumption is that this will probably lead to a marked decline in the aggregate savings ratio[9]

Moreover, increasing inequality of income distribution may well have contributed to an increase in the savings ratio, as households with markedly above-average income have above-average savings ratios. In Germany income inequality was relatively stable during the 1980s and 1990s as measured by the Gini coefficient. Since the turn of the millennium and especially in the years preceding the financial and economic crisis it has risen significantly, albeit rather moderately by international standards. Chart 10 shows a positive correlation between the Gini coefficient and the savings ratio, which supports the argument

[9] ZEW (2012). Sparen und investieren vor dem Hintergrund des demographischen Wandels, Endbericht an das Bundesministerium der Finanzen.

presented here. However, the savings ratio moved within a very narrow range during this period, so the effect is likely to be on the minor side.

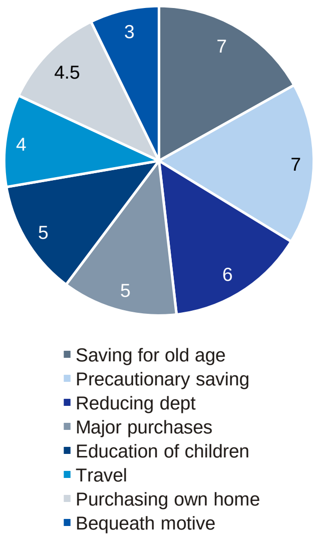
Thrift as a value in a child's upbringing (share of "Important" responses) 11



Source: World Value Survey

Saving motives 12

Scale from 0-10 points



Source: Household Finance and Consumption Survey

Surveys – Saving remains important despite zero interest rates

As part of the World Value Survey respondents are asked whether "thrift" is considered an important value in a child's upbringing. This opinion is shared by over 40% of respondents in Germany, which is about 10 percentage points above the international average. According to a Bank of Scotland survey published in 2014 a majority of German households (60%) save regularly. This is high by European standards. However, 26% of German households save only occasionally and 14% do not save at all. The motives for saving by household can be broken down as follows: according to the Household Finance and Consumption Survey (HFCS) for the period 2011-2012 the primary motives for saving among European households are for old age and for unforeseen circumstances. This tallies with a survey of German households: according to the findings of the SAVE study from 2003 until 2010 providing for old age and building a reserve for unforeseen events are the most important motives for saving by households, commanding seven out of ten points. This corresponds with the life cycle hypothesis and shows that Germans – on account of being highly risk averse – will probably maintain a minimum level of current savings despite the extremely low interest rates.

Another motive is reducing indebtedness, which receives a weighting of six out of ten points. By contrast, major purchases and children's education garner a weighting of five points. Travelling and one's own home with weightings of four points and four-and-a-half points respectively are of relatively little importance. The bequeathing motive is only rated with three out of ten points and thus has the lowest weighting. On average the importance of saving has risen over time, which appears to contradict the aggregate savings ratio trend.

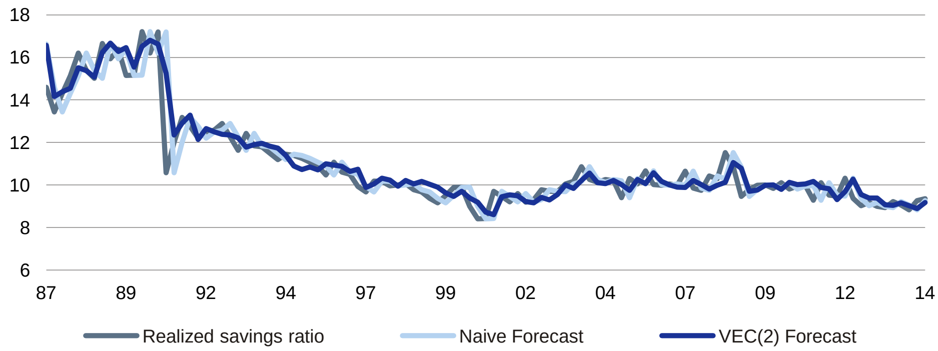
In the current low interest rate environment 64% of households regard interest rates as being generally too low, according to a survey by Gothaer Asset Management. However, Germans' actual saving and investment decisions display considerable inertia. Current developments in the capital markets influence saving to only a small degree, as the econometric model will also show. Consequently a mere 4.4% of respondents own shares. The majority invest their savings in instant access deposit accounts (39.7%) and in fixed-term deposit accounts (18.4%). This strong "status quo bias" is probably the result not least of a very strong aversion to risk (loss): in a GfK consumer survey published in 2013, 91.6% of respondents stated that they are not prepared to take greater risks to share in potential gains in the capital market.

A simple explanatory model shows that interest rates exert only minor influence

Given the multiplicity of factors it seems pointless to try and develop a complete econometric model to determine the savings ratio. We shall therefore restrict ourselves to examining the long-term relationship between income and consumption, which yields the saving as the residual amount, supplemented by short-term factors that influence the relationship between consumption and income. Here we make use of the fact that budget restrictions mean there should be a close correlation between disposable income and consumption expenditure. The difference between the two variables corresponds to the amount saved. It should therefore be assumed that consumption and disposable income are cointegrated, i.e. they follow a shared stochastic process. We can confirm this via our tests.

Actual vs forecast of the savings ratio for every quarter 13

in %



Source: Federal Statistical Office Germany, Deutsche Bank Research

Deviations from the long-term equilibrium between disposable income and consumption subside over time, but they are never constant. We have integrated the corresponding error correction equation into a vector auto-regressive model in order to test the influence of other variables on the interplay between disposable income and consumption. A significant influence on the current savings ratio is exerted by consumption in the period before last, the change in disposable income, the growth in gross domestic product, the change in the consumer price index and the total dependency ratio, which is defined here as the ratio of under-15s and over-64s to the group of potentially economically active group of 15-to-64-year-olds (lagged in each case).

Thanks to the auto-regressive structure of our model a decline in consumption in the preceding two quarters leads to an increase in the current period and thus to a smaller amount being saved, i.e. a declining savings ratio. Accordingly, shrinking disposable income in the preceding periods has the opposite effect and thus makes the savings ratio increase. A decline in the overall dependency ratio leads to rising disposable income in the model and thus an increase in the savings ratio. The increase in the overall dependency ratio, which will accelerate markedly over the next few years, is thus likely to result in a “structural” decline in the savings ratio in future. Interest rate changes have an impact on saving, albeit of only minor statistical significance. Falling interest rates tend to lead to a lower savings ratio, though.

Our time-series model explains an adjusted 13.7% of the variability in the savings ratio (adj. R^2) and thus beats naive, univariate and multivariate time-series benchmarks with and without cointegration based on the mean square error.

Vector Error Correction Estimates 14

Date: 02/25/15 Time: 16:02
Sample (adjusted): 1981Q1 2014Q3
Included observations: 135 after adjustments

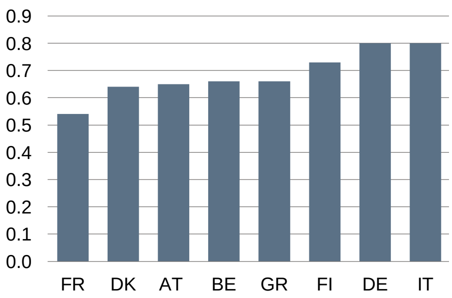
Cointegrating Eq:	CointEq1	
CONSUMPTION(-1)	1	
DISINCOME(-1)	-0.961557 ***	
C	21.15482	
Error Correction:	**D(CONSUMPTION)**	**D(DISINCOME)**
CointEq1	-0.123315 *	0.239139 **
D(CONSUMPTION(-1))	-0.154117 *	0.188445 *
D(CONSUMPTION(-2))	-0.007641	0.18866 *
D(DISINCOME(-1))	-0.088834 *	-0.284357 **
D(DISINCOME(-2))	-0.119621 *	-0.253235 **
C	2.131293 ***	1.685128 ***
D(GOVBONDYIELD(-3))	0.289131	-1.188021 *
D(GDP(-2))	0.687109 ***	0.895057 **
D(Consumer_Prices(-2))	1.088364 ***	1.312078 **
D(AgeDR(-1))	-0.80589	5.905022 ***
R-squared	17.2%	21.6%
Adj. R-squared	11.25%	15.98%

*** = significant with alpha=1%
** = significant with alpha=5%
* = significant with alpha=10%

Source: Deutsche Bank Research

Germans are risk averse 15

Variable: Risk aversion



Source: "Risk preferences around the World" (M. Rieger, M. Wangy, T. Hensz), Sep 26, 2013

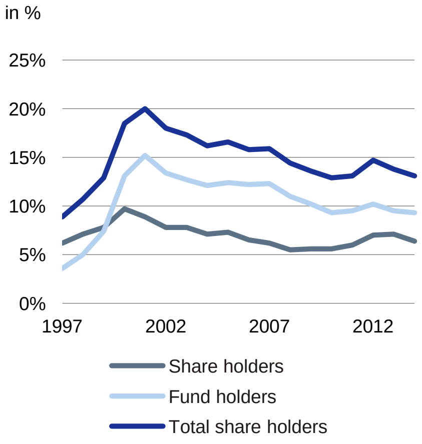
Behavioural economics: Status quo bias and risk aversion

Both the restrictive "Homo economicus" assumptions[10] from the theoretical models as well as the purely quantitative approach of our model ignore the psychological component of the decision to save. Given the incomplete information, limited cognitive resources, systematic decision-making errors and the limited opportunity to learn from past mistakes – due to the often large timelag between decision and result – the decision to save is truly a perfect example of the influence of behavioural economic factors[11].

The "status quo bias", the tendency to remain entrenched in existing behavioural patterns, suggests that the savings ratio does not react noticeably to low interest rates. The above-mentioned explanation that savings behaviour is largely determined ex ante points towards a similar conclusion. The status quo bias is particularly pronounced in situations of increased uncertainty. It can be assumed that the unconventional monetary policy, which is increasingly difficult for laypeople to understand, and the role of the ECB in the political conflicts in the eurozone, have led to an increasing wait-and-see attitude among average investors. This phenomenon is described in behavioural economics as "loss of competence". The strong risk aversion of German households is probably at odds with the portfolio rebalancing reaction intended by the monetary policy of zero interest rates and quantitative easing. This means switching from lower and lower yielding low-risk investments (fixed-term deposits, Bunds) to more risky assets. Although already in 2014 the interest rates on sight deposits and Bund yields fell to record lows and the Dax continued to climb sharply as many had expected, the number of Germans who

[10] Schneider, Stefan (2010). Homo economicus – or more like Homer Simpson? Deutsche Bank Research. Current Issues, June 29, 2010.
[11] Melissa A.Z. Knoll (2010). The Role of Behavioral Economics and Behavioral Decision Making in Americans' Retirement Savings Decisions.

Share and funds holder in % of total population 16



Source: Deutsches Aktieninstitut

own shares directly or via funds fell by 500,000 in 2014 and thus the share ratio dropped to 13.1%. In particular the percentage of those directly owning shares fell by about 10% to 4.1 m (ratio 6.4%)[12]. However, the scepticism about the financial system combined with the numerous reports of rising (booming) property prices is leading to higher demand for property from Germans. This would at least be implied by the so-called "availability heuristic", according to which news gains a greater influence on decisions as long as it is simply repeated often enough. However, the current growth rate for mortgage loans of around 3% yoy does not currently point towards any significant change in behaviour. Unfortunately it is not observable to what degree the decline in the interest rate level that has been ongoing for years has led to an adjustment of the reference point for investment decision-making. The reference point is the subjective assessment that defines the line between profit and loss from the investor's point of view. If one assumes that in the zero interest rate environment capital retention has become the new reference point for many investors, according to the "prospect theory"[13] capital losses are felt much more strongly than a corresponding capital gain (loss aversion). This may explain why investors make do with zero interest rates instead of trying to achieve a higher return via riskier investments.

Conclusion: Interest rates have only a minor influence – but savings ratio will continue falling for demographic reasons

All in all, economic theories trying to explain households' savings behaviour and the impact of interest rates can only be partly corroborated by empirical evidence. Neither can surveys or behavioural approaches provide clear-cut evidence regarding the impact of zero interest rates on the household savings ratio. Although our model finds a slightly negative correlation, the VAR methodology means it is not really suitable for forecasting over an extended period. In addition, the relationship between interest rate and savings behaviour might not be linear close to zero. Currently, the decline in the inflation rate due to the Pigou effect could result in another temporary decline in the savings ratio. In addition, the relatively sizeable residential property investments that households are likely to make for a number of years together with further rising prices via corresponding writedowns will probably continue to exert pressure on the net savings ratio. In the medium term the dissaving of the baby boomers who will then have retired will probably lead to another marked decline in the savings ratio. All in all, it is fair to assume that predictions of a further decline in the German savings ratio resulting from the ECB's zero interest rate policy will be right, although for the wrong reasons.

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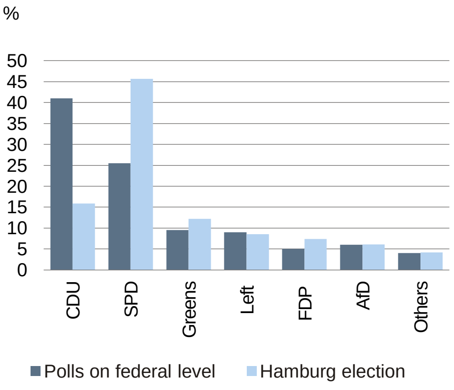
Niels Wesselhoefft

[12] Deutsches Aktieninstitut (2014). Aktionärszahlen des Deutschen Aktieninstitutes 2014.
[13] Kahnemann, Daniel (2011). Thinking, fast and slow.

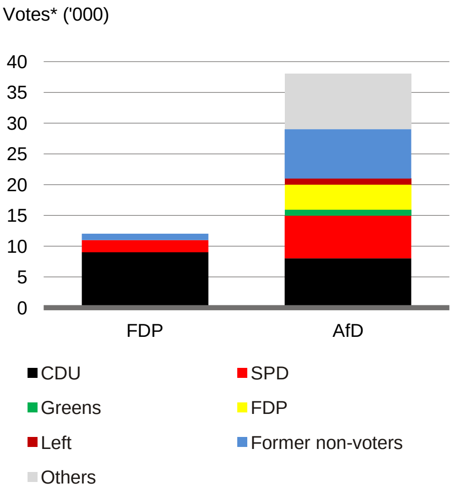
The view from Berlin

Result of the Hamburg election vs recent polls on the federal level 1



Sources: Allensbach Institute, Landeswahlleiter

Hamburg election: Voter transitions 2



* Number of FDP/AfD voters who formerly voted for ...

Source: Infratest dimap

Election calendar 3

May 10, 2015	State election	Bremen
Spring 2016	State election	Saxony-Anhalt
Spring 2016	State election	Baden-Wuerttemberg
Spring 2016	State election	Rhineland-Palatinate
Autumn 2016	State election	Berlin
Autumn 2016	State election	Mecklenburg-West Pomerania
…		
Autumn 2017	Federal election	

Source: Wahlrecht.de

Shift in Germany's political landscape?

National politics is still happening despite the hype about Greece – and might have a more lasting effect. The recent state election in Hamburg in a sense confirmed a trend that is indicated by polls on the federal level: there is absolutely no mood for a change at the moment. Nevertheless, debates on the election's impact on federal politics have started. Given the CDU's deep fall and the FDP's as well as the AfD's success in passing the 5% threshold and taking seats in the city parliament, commentators speculate on fundamental changes in Germany's political landscape. Such reasoning would be premature, however.

Hamburg's ruling SPD mayor, Olaf Scholz, and his party were able to surf the mood for continuity. Capturing 45.7% of the vote, the SPD matched its average from all 20 elections there since 1946 (45.4%). Scholz – formerly an SPD secretary general and federal labour minister – was rewarded for his business-friendly record. This is a bitter pill for the SPD's left-wingers who advocate a coalition with the Left Party and the Greens in Berlin. Scholz's success might also question Economy Minister Gabriel's run for chancellor in 2017.

Federally, the widespread desire for stability benefits Chancellor Merkel. In particular, the majority of Germans embrace the government's main principles on euro-area policy, i.e. fiscal support only in return for reform efforts, and back her policy towards Russia. Her popularity as well as the CDU's approval rates (about 41%) have stayed high, while in Hamburg the CDU suffered a historic defeat (15.9%). Merkel has shrugged this off as a local event. However, the CDU cannot ignore that it matches the series of poor showings regionally, with the CDU now heading only 4 state governments (and the CSU one) out of 16. But state administrations have always been a power base and a political talent source. So there are doubts whether the CDU could prevail as the chancellor's voting association only.

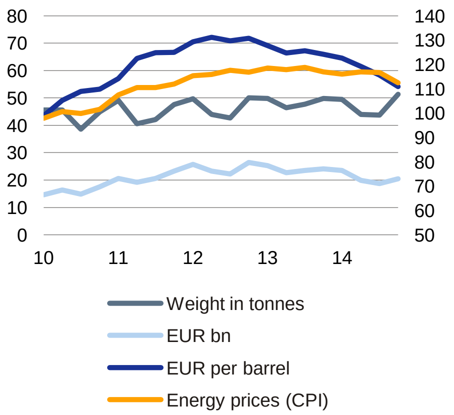
In Hamburg the CDU's pain was the smaller parties' gain. The FDP has ended hard times there. Since spring 2013 that party has suffered several heavy defeats. But it seems questionable whether the FDP has already turned the corner. In Hamburg it strongly focused its campaign on its agile top candidate, Katja Suding, but also addressed business issues. Thus, it managed to attract more votes from the CDU than any other party. The AfD took seats in a west German state parliament for the first time, after its recent success in three east German elections. The AfD, too, benefited from the CDU's weakness, but it gained nearly as many votes from the SPD. Nevertheless, the AfD was unable to substantially leverage a favourable political setting in Hamburg: this is the home of its party leader, and the euro-sceptics should have cashed in on the ongoing migration debate and even more so on events concerning Greece. So is not the sky but the relatively meagre 6.1% from Hamburg the AfD's limit?

For the AfD as well as the FDP the litmus test will be the Baden-Wuerttemberg election in spring 2016, when 12% of German voters will be called to the polls (instead of 2% as in Hamburg). There, both parties are likely to focus their campaign on issues to which Merkel's CDU has attached only secondary importance so far, namely tax policy and deregulation as the FDP's favourite topics, and support for families and (alleged) immigration into the social systems to mention the AfD's major issues besides its euro-sceptic attitude. In many voters' eyes the CDU has traditionally shown competence in these fields. If this no longer holds true in future, Germany's political landscape could change indeed.

Barbara Böttcher (+49 69 910-31787, barbara.boettcher@db.com)

Chart of the month

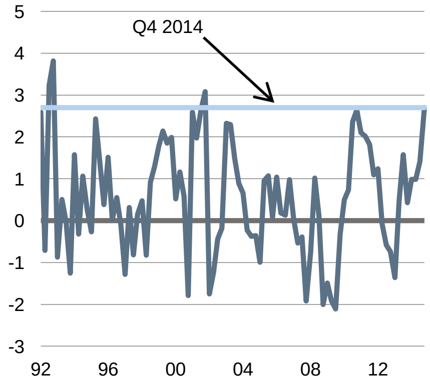
Oil and gas imports



Sources: Federal Statistical Office, Deutsche Bank Research

Real disposable income growth

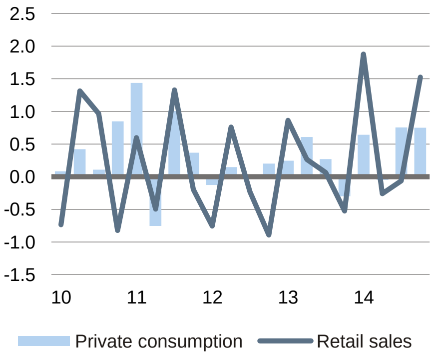
% yoy, deflated with consumer prices



Sources: Federal Statistical Office, Deutsche Bank Research

Strongest 2-quarter consumption growth since 2010

Real, % qoq, sa



Source: Federal Statistical Office

Oil price drop drives real incomes and consumption

The massive oil price decline provides a "stimulus package" for oil importing countries. From Q2 2013 to Q2 2014 oil had traded roughly stable at EUR 74 per barrel. In Q3 2014 it fell to EUR 67 only to drop even further to below EUR 50 in the final quarter of the year – a cumulated decrease of over 30%. At least in part due to its disinflationary effect about 20 central banks worldwide have loosened monetary policy lately.

The development of the oil price lowered Germany's oil bill by about EUR 4 bn or 20% – equal to 0.5% of quarterly GDP. While the quarterly import bill amounted to EUR 24 bn in the 2 years before the price drop, it averaged EUR 20 bn in the last three quarters – and that despite a marked volume increase (in tonnes) in Q4.

Import prices began to soften in Q2 2014, but consumers only started to benefit in the last quarter of 2014, according to the energy component of the CPI. This fell by 3.6% qoq in Q4. With energy standing for about 10% of a consumer basket, consumers could devote about 0.4% of their nominal spending to other uses. The already substantial uptrend in nominal disposable incomes was reinforced in real terms thanks to this oil price effect. Real disposable incomes grew by 1.3% qoq (2.7% yoy) – the highest rate since 2006 (and 2001). Real private consumption thus rose by 0.8% qoq – as in Q3 – making H2 2014 the strongest two-quarter period since 2010, when the economy was recovering from the crisis. In addition, real retail sales showed the second strongest growth rate of the last 20 years.

We expect that (real) private consumption will continue to receive impetus from falling oil prices in early 2015. So far the price has dropped another 25% compared to Q4, despite the recent stabilisation. This adds to the already strong income growth, courtesy of the ongoing labour market strength. Furthermore, the Q4 increase in the savings rate to 9.8% (after having averaged 9.1% in the previous 8 quarters) was probably an unintended side-effect of the windfall gains provided by the oil prices slump. A reversal should therefore be expected.

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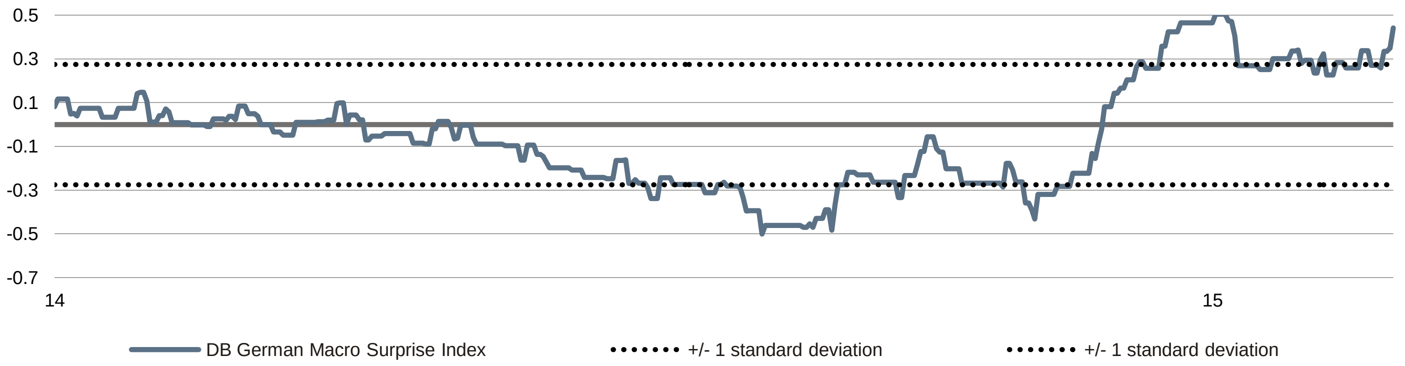
DB German Macro Surprise Index

The DB German Macro Surprise Index compares published economic data with market forecasts and thus provides clues as to the direction of future forecast revisions.[14]

DB German Macro Surprise Index

Average of last 20 z-scores of data surprises



Values above (below) 0 indicate the data came in better (worse) than expected

Sources: Bloomberg Finance LP, Deutsche Bank Research

Last 20 published economic data for Germany

Bloomberg Tickers	Indicator	Reporting month	Publication date	Current value	Bloomberg consensus	Surprise	Standardised surprise	Quantile rank
GRZEWI Index	ZEW Survey Expectations	1 2015	20.01.15	48.4	40.0	8.4	1.0	0.8
GRIFPBUS Index	IFO Business Climate	1 2015	26.01.15	106.7	106.5	0.2	0.0	0.5
GRIMP95Y Index	Import Price Index (% yoy)	12 2014	28.01.15	-3.7	-3.4	-0.3	0.1	0.5
GRUECHNG Index	Unemployment Change (000's mom)	1 2015	29.01.15	-10.0	-10.0	0.0	-0.2	0.4
GRFRIAMM Index	Retail Sales (% mom)	12 2014	30.01.15	0.6	0.3	0.3	0.5	0.7
MPMIDEMA Index	Markit Manufacturing PMI	1 2015	02.02.15	50.9	51.0	-0.1	-0.1	0.4
MPMIDESA Index	Markit Services PMI	1 2015	04.02.15	54.0	52.7	1.3	1.4	0.9
GRIORTMM Index	Factory Orders (% mom)	12 2014	05.02.15	4.2	1.5	2.7	1.2	0.9
GRIPIMOM Index	Industrial production (% mom)	12 2014	06.02.15	0.1	0.4	-0.3	-0.2	0.4
GRCAEU Index	Current Account Balance (EUR bn)	12 2014	09.02.15	25.3	20.8	4.5	1.0	0.8
GRCP20YY Index	CPI (% yoy)	1 2015	12.02.15	-0.4	-0.3	-0.1	-0.3	0.2
GRZECURR Index	ZEW Survey Current Situation	2 2015	17.02.15	45.5	30.0	15.5	2.1	1.0
GRZEWI Index	ZEW Survey Expectations	2 2015	17.02.15	53.0	55.0	-2.0	-0.2	0.4
MPMIDEMA Index	Markit Manufacturing PMI	2 2015	20.02.15	50.9	50.9	0.0	0.0	0.5
MPMIDESA Index	Markit Services PMI	2 2015	20.02.15	55.5	55.5	0.0	0.0	0.5
GRIFPBUS Index	IFO Business Climate	2 2015	23.02.15	106.8	107.7	-0.9	-0.8	0.2
GRGDPPGQ Index	GDP (% qoq)	12 2014	24.02.15	0.7	0.7	0.0	-0.1	0.3
GRUECHNG Index	Unemployment Change (000's mom)	2 2015	26.02.15	-20.0	-10.0	10.0	0.2	0.6
GRCP20YY Index	CPI (% yoy)	2 2015	27.02.15	0.1	-0.3	0.4	2.5	1.0
GRIMP95Y Index	Import Price Index (% yoy)	1 2015	27.02.15	-4.4	-4.6	0.2	0.5	0.8

Sources: Bloomberg Finance LP, Deutsche Bank Research

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[14] See for details Focus Germany. August 4, 2014.

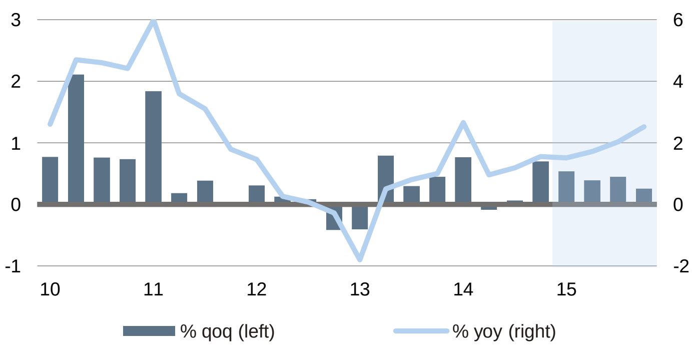
Chartbook – Total economy

— After stagnation during summer, the German economy accelerated markedly to 0.7% qoq in Q4 2014 – the strongest quarterly growth among the largest industrial countries. GDP grew by 1.6% on an annual average in 2014. This is a marked acceleration relative to the weak economic growth seen in 2012 (+0.4%) and 2013 (+0.1%). Main growth driver was private consumption thanks to the good shape of the labour market. The number of employed persons increased to the historical peak of 42.7 million and disposable income grew by a solid 2.4%. Investments expanded only moderately due to elevated geopolitical risks and disappointing world trade. Net exports also contributed to GDP growth.

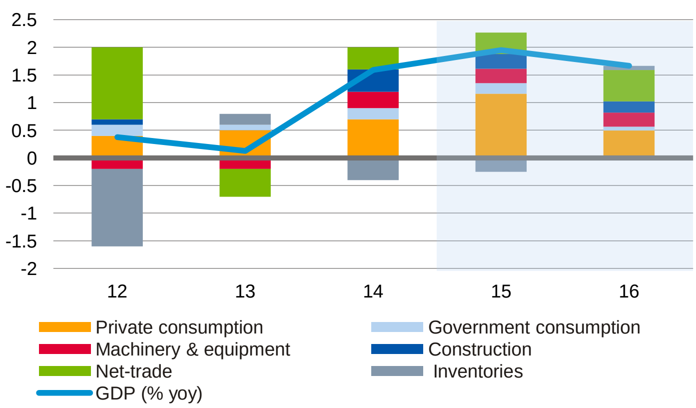
— Sentiment indicators improved recently. They are pointing to strong GDP growth in Q1 2015 of about ½% qoq. Favourable for the German economy are the slump of oil prices and the strong depreciation of the EUR. The ongoing elevated geopolitical risks – esp. the Ukraine-Russia crisis – continue to be a drag. The ifo index increased for the fourth month in a row in February. The composite PMI increased strongly driven solely by the services component.

— We lifted our GDP growth forecast for 2015 thanks to the higher starting level for 2015 provided by Q4, the slump of oil prices and the weakening of the EUR. We now expect the German economy to expand by 2.0% in 2015 and 1.7% in 2016.

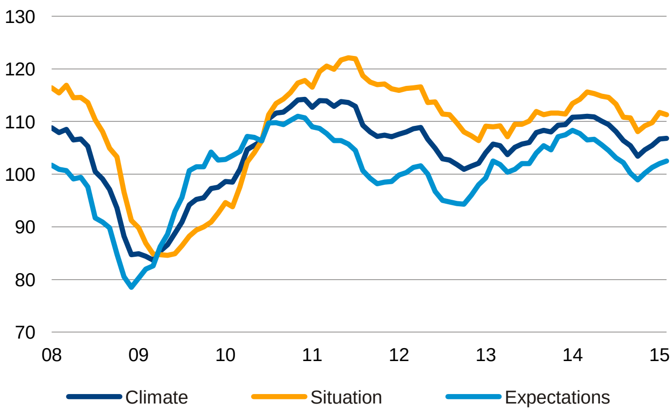
Real GDP growth



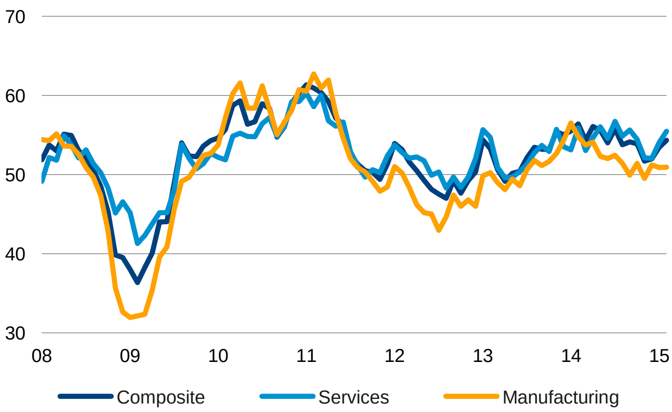
Contribution to real GDP growth (%-points)



ifo index - total economy (2005=100)



Purchasing manager index



Sources: Federal Statistical Office, Markit, ifo, Deutsche Bank Research

Chartbook – Foreign trade

— German trade numbers surprised to the upside in December. Exports were up by almost 4% mom which pushed the volatile year-on-year rate to almost 10%. The weakness of oil prices left its imprint in imports which fell by a slight 0.2% mom (4% yoy). Therefore, the trade balance was up to EUR 22 bn.

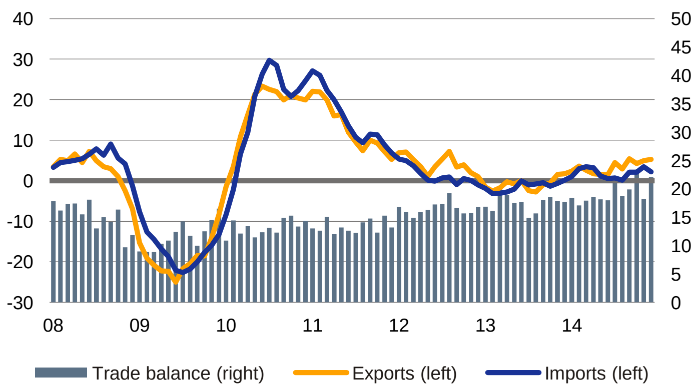
— The 3 months average showed a 5% yoy export increase. Demand from the US and Asia remained high and exports to these destinations were up 9% yoy (3M mov. avg.) and 8%, respectively. Exports to EMU dampened (+3%).

— Growth of automobile exports was relatively strong with 8% yoy (3M mov. avg.). Due to one-offs (holiday effect, re-tooling of production lines for new models) the monthly volatility was elevated in recent months. Export growth of the electrical engineering industry was up by 6% yoy, followed by mechanical engineering (+1.5%), chemicals (+0.6%) and the metal industry (-0.2%).

— Leading export indicators increased in February, but remained on a relatively low level pointing to a modest development in the coming months. The unresolved Ukraine-Russia crisis and the clouded growth outlook for major German trading partners – esp. China, France, Italy – will probably continue to be a drag. Thanks to the moderate recovery of the world economy in the further course of this year and the weaker EUR, we expect a gradual recovery of exports. Imports will probably grow relatively strongly thanks to robust domestic demand.

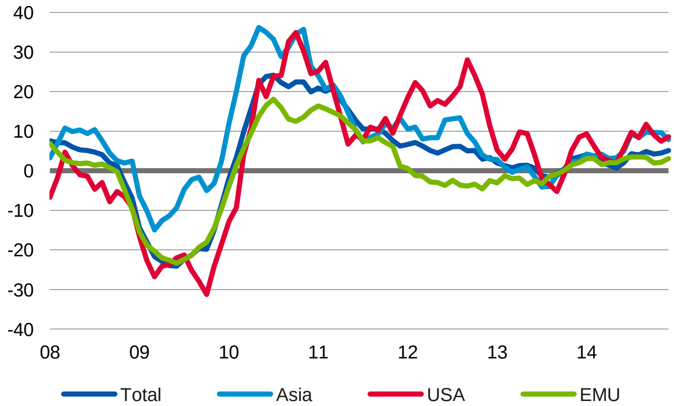
Merchandise trade

% yoy, 3M mov. avg. (left); EUR, bn (right)



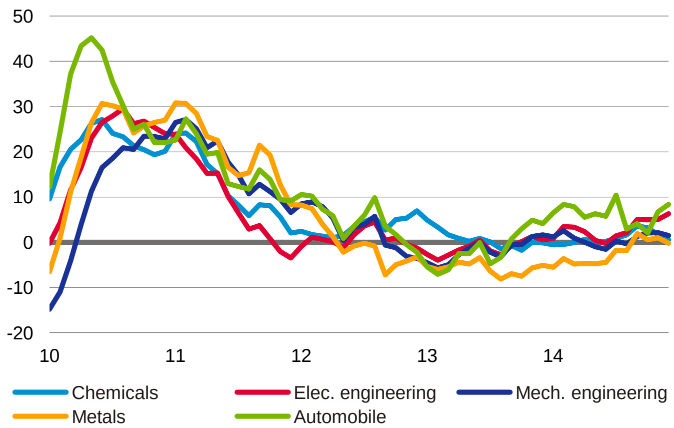
German exports by region

% yoy, 3M mov. avg.



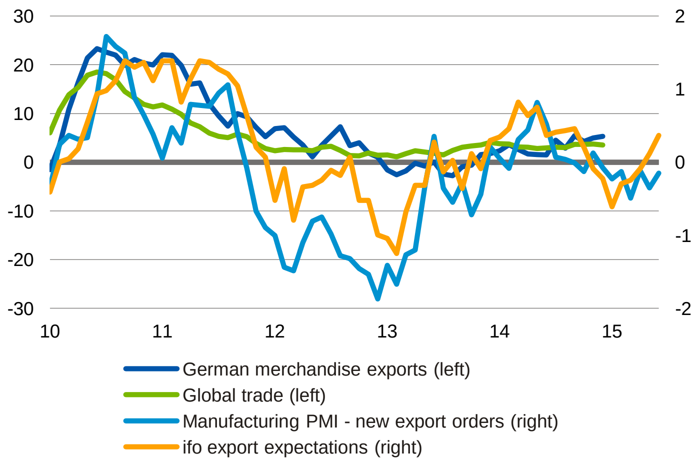
Exports by sector

% yoy, 3M mov. avg.



Exports and early indicators

% yoy, 3M mov. avg. (left); Standardized values (right, 4M lead)



Sources: Federal Statistical Office, Markit, ifo, Deutsche Bank Research, CPB

Chartbook – Industry

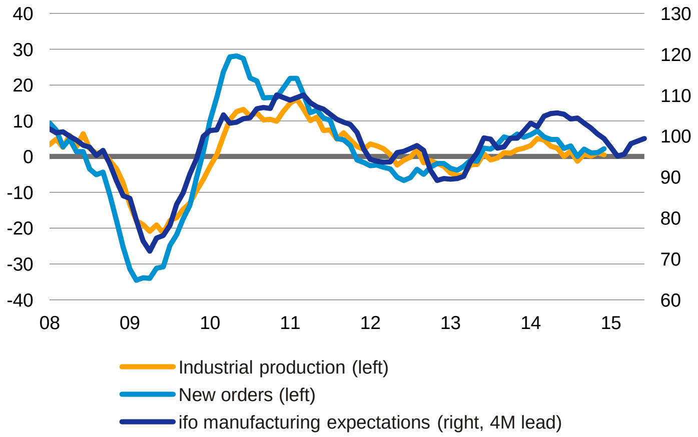
— Industrial production disappointed somewhat in December by increasing only 0.1% mom. However, the construction sector’s decline (-2.9%) overshadowed the positive impetus from the fourth consecutive output increase in the manufacturing sector.

— The improvement in the manufacturing ifo and PMI as well as the further rise of capacity utilization in Q1 all point to a continuation of the industrial recovery, though they all are only consistent with moderate output growth in Q1.

— In the course of 2015 industrial production in Germany is likely to record an uptrend. The weaker EUR and falling oil prices provide significant impetus. We expect German industrial production to increase by 1.5% in 2015 in real terms (2014: 1.9%). Somewhat stronger than expected production results in Q4 2014 support our assessment. We expect both the automotive industry and mechanical engineering to increase their output by roughly 2% in 2015. While mechanical engineering should thus improve its performance over 2014 (+0.8%), the auto industry should see its growth cool (2014: +4.5%). Production in the electrical engineering industry is expected to grow by 1.5% – following a 2.5% increase in 2014. Production in the metals industry is expected to increase by more than 1% in 2015 after a relatively strong plus last year (+3.2%). Chemicals production is likely to add 1.5% in 2015; however, this would not neutralise the setbacks in 2014 (-2.9%). Food production could increase by 0.5% in 2015 (2014: +0.1%).

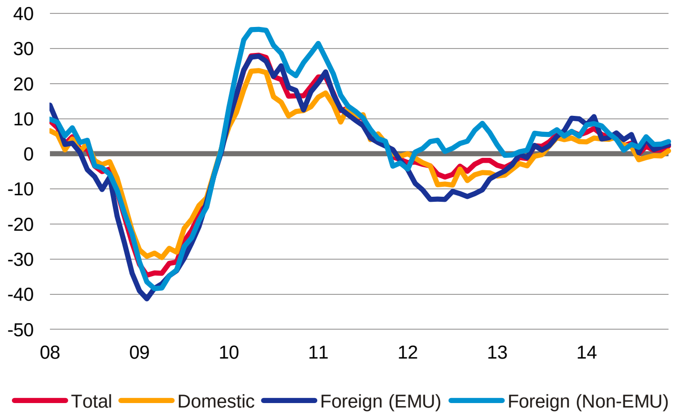
Industrial production, new orders & ifo expectations

% yoy, 3M mov. avg. (left); index (right)

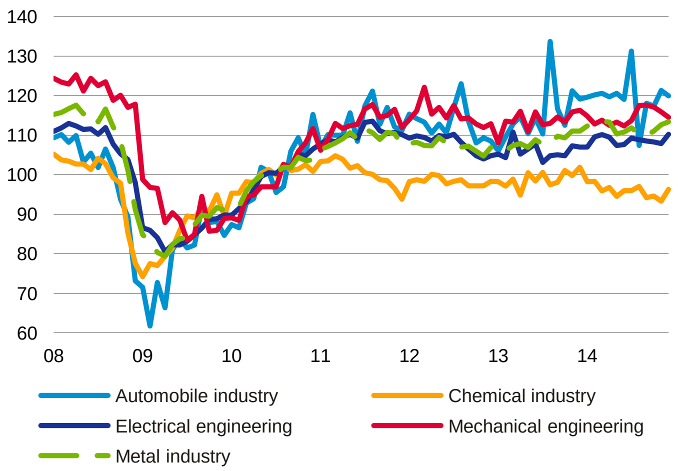


New manufacturing orders by region

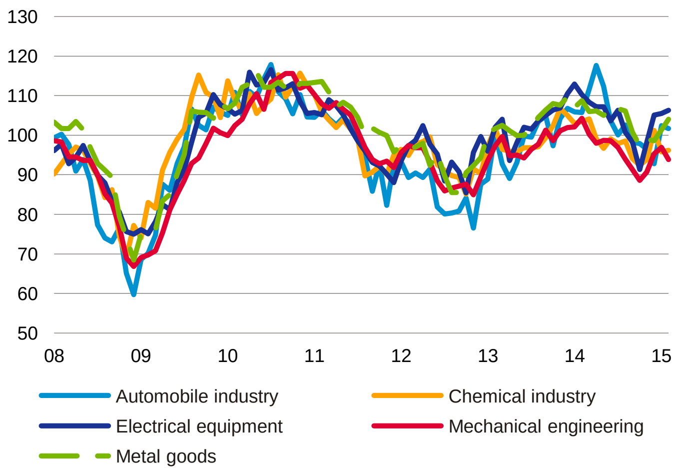
% yoy, 3M mov. avg.



Production of largest industrial sectors (2010=100, sa)



ifo business expectations of the largest industrial sectors (2005=100)



Sources: Federal Statistical Office, ifo

Chartbook – Domestic economy

— The German labour market showed ongoing strength in February. Unemployment was down (-20k mom). Strong employment growth continued to be mainly driven by the integration of immigrants into the German labour market which highlights mismatch problems of the domestic labour force. The outperformance of employment relative to unemployment continues due to somewhat above 300,000 additional persons having entered the German labour market mainly thanks to high net migration. Early indicators suggest a positive development over the next few months. During the rest of the year the likely negative impact from the minimum wage on employment will become more and more visible. The unemployment rate should fall to 6.5% in 2015 (2014: 6.7%).

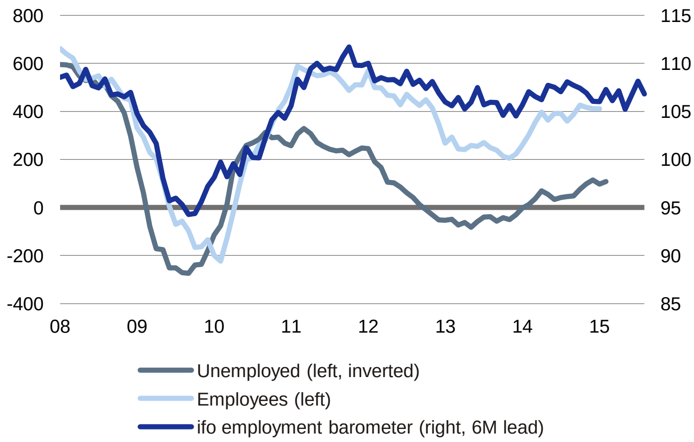
— Real retail sales rose in December (+0.6% mom). It was the third consecutive increase bringing Q4 sales up by a strong 1.5% qoq. Continuous employment build-up, solid wage increases and the falling oil price all contributed to this. The 4% jump compared to December 2013 was in part due to 2014 one additional working day. All told, retail sales rose by 1.5% in 2014 and thus somewhat stronger than private consumption (+1.2%), which only happened four times since 1995. Consumer confidence indicators have turned late-2014 and suggest a continued moderate uptrend in sales.

— Investment in machinery & equipment and construction spending are expected to contribute to growth in 2015. Domestic investment goods orders and capacity utilization currently point to a moderate recovery in Q1. During the rest of the year, we expect investment in M&E to pick up and to grow by 3.8% on annual average in 2015.

— The construction sector benefits from high net immigration and rising disposable income propelling housing demand. Construction spending could grow by about 2.7 % in real terms in 2015. But monthly indicators for construction activity were relatively weak recently despite robust business sentiment.

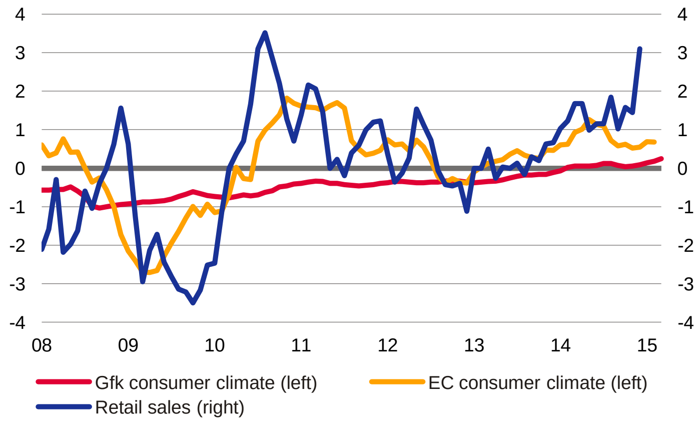
Unemployment barometer, employment and unemployment

'000 yoy (left); index (right)



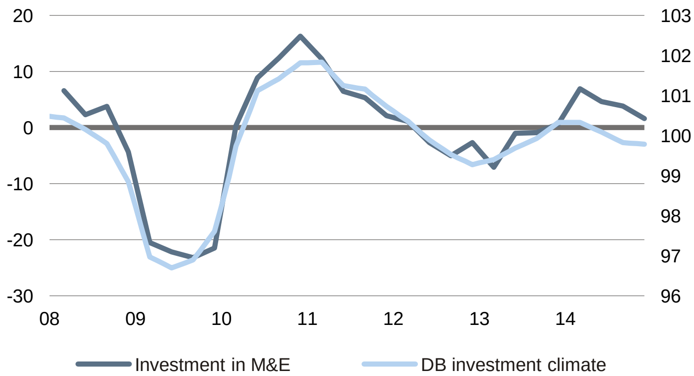
Retail sales and consumer confidence

Normalized data (left), % yoy, 3M mov. avg. (right)



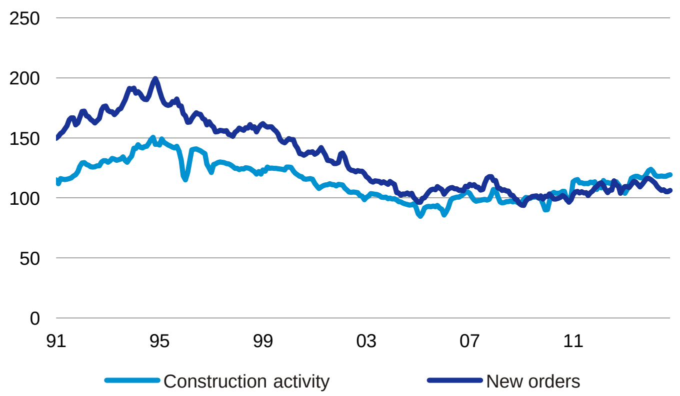
Investment in machinery & equipment and DB investment climate

% yoy (left); index normalized to 100 (right)



Construction activity and new orders

2010=100, 3M mov. avg.



Sources: Federal Statistical Office, Deutsche Bank Research, Gfk, EU Commission, ifo

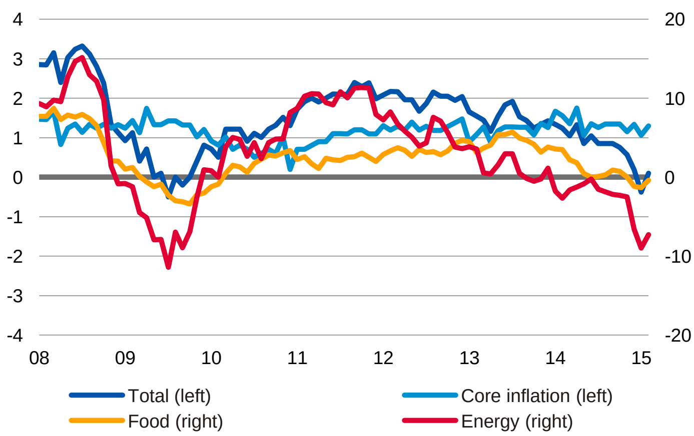
Chartbook – Financial markets

— After a temporary dip below zero German inflation recovered in February. According to preliminary information the inflation rate stood at 0.1% yoy after -0.4% previously. Thanks to the partial recovery of oil prices energy prices were less negative in yoy-terms compared to January (-7.3% vs -8.4% prev.). Food prices also rose (-0.4% yoy vs -1.3%). As expected core inflation recovered in February likely to 1.3% after it had fallen to 1.1% in January. It is likely to have benefited from the rebound in prices for package holidays. Over the next months inflation is likely to hover near 0% due to ongoing weakness of energy prices. In contrast, core inflation could potentially receive some impetus from second-round effects due to the introduction of the minimum wage in January 2015.

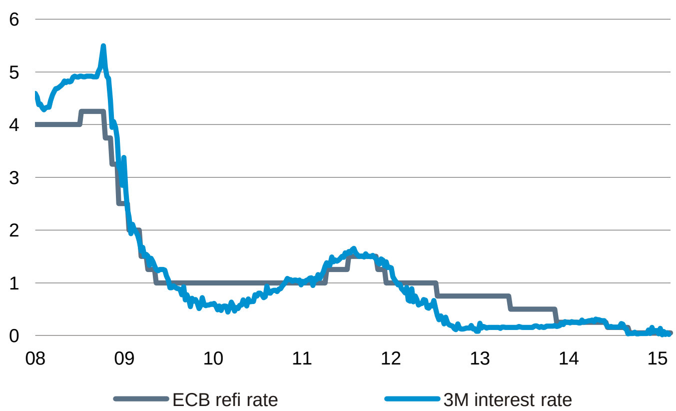
— Fearing a negative feedback loop between declining current inflation, a disanchoring of inflation expectations and the still weak banking system restricting the supply of credit, the ECB decided at its meeting in January to extend its asset purchases significantly and to lower the interest rate for the TLTROs. Starting in March, the ECB will buy bonds issued by euro area central governments, agencies and European institutions in addition to the already started purchases of covered bonds and ABS. The total purchase volume will be EUR 60 bn per month and run at least until September 2016. Objectives are credit easing and weakening the EUR by expanding the balance sheet by EUR 1.1-1.2 trillion.

— Given the extremely expansionary monetary policy stance of the ECB interest rates of 10Ygovt. bonds declined further. The yield for 10Y German govt. bonds fell significantly to currently below 0.4%. The yield spread between 10Y US treasuries and German Bunds was 1.8 pp as of late.

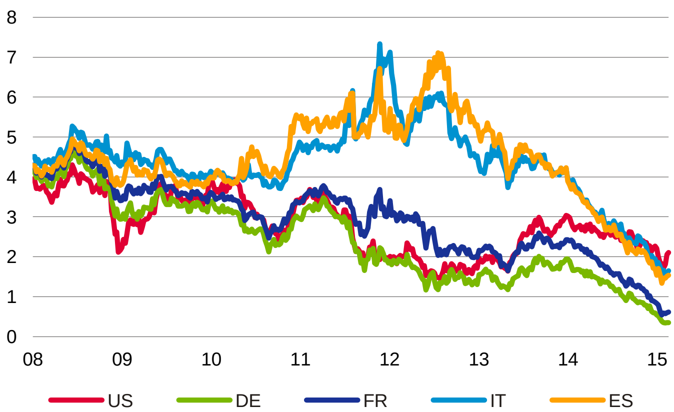
Consumer prices (% yoy)



EMU: Refi rate & 3M interest rate (%)

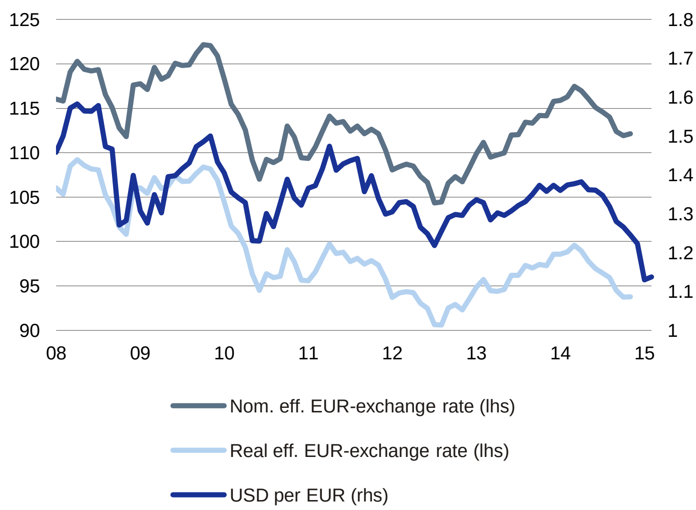


10Y government bond yields (%)



Exchange rate development for the EUR

1999Q1=100 (left), USD per EUR (right)



Sources: Federal Statistical Office, ECB, EU Commission, Global Insight, Reuters, Deutsche Bank Research

Chartbook – Lending

— Credit to corporates in the euro area has been shrinking since March 2012. January 2015 also saw a further drop (-1.6% yoy). However, during 2014 reductions have become less and less pronounced (for comparison: Jan 2014: -3.4%, mid-2013: -5.9%). Smaller reductions of course reflect the accumulated cuts which have already taken place as well as improving growth prospects for the euro area.

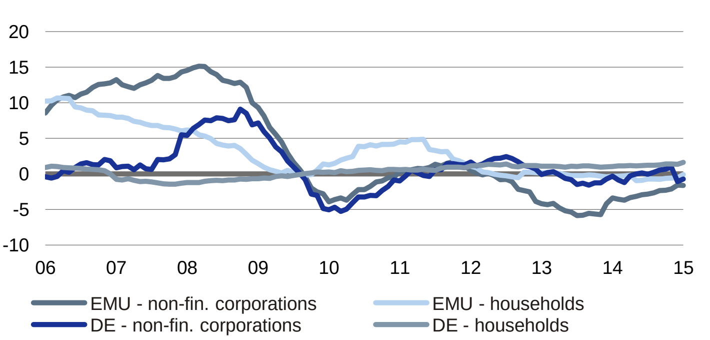
— Credit to households in the euro area remained stable in January 2015 (-0.1% yoy). Here, shrinking has become less pronounced during the 2nd half of 2014 (Dec: -0.5% yoy compared to -0.8% in July 2014).

— Credit conditions for German corporates continue to be very favourable. Interest rates for corporate credit are at 2.8% (December). In January 2015 the share of companies reporting restricted access to credit reached a new record low. Only 17.1% of companies from industry and trade (Dec.: 17.4%) report restrictive access to credit. Similarly, credit conditions for construction companies are very benign (20.9% reporting restrictive access after 21.5% in Dec.). Access to credit is substantially easier than 5 years ago when the shares of corporates reporting restrictive access were more than twice as high. Despite the very good conditions, credit growth remained subdued in 2014. After slight growth in yoy comparison in autumn, latest drops however also reflect statistical reclassifications (Jan. 2015: -0.8%, Dec.: 1.1%). The restrained demand for credit by German corporate also reflects the rise of alternative financing options such as issuing corporate bonds where volumes have more than doubled since 2008.

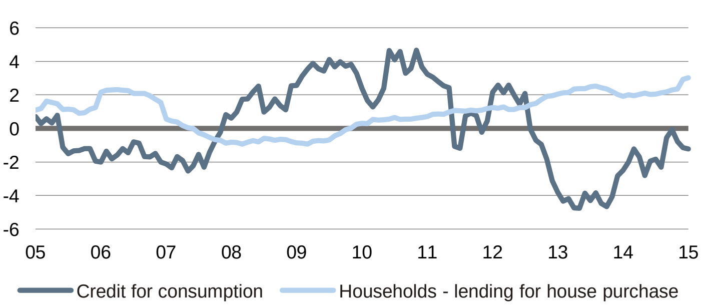
— Lending to households in Germany continues to rise modestly (Jan.: +1.6% yoy). Growth in mortgage credit continues to drive total increases and has been picking up somewhat driven by the further drop in interest rates (new record low for mortgage rates in Dec. at 2.1%) during the second half of the year. This trend seems to continue and January saw an increase to 3% yoy for the first time.

— Given the very low interest rates increases overall credit growth might still appear rather moderate. Rising real incomes reduce the need to finance consumption via credit for many households translating into moderate credit demand despite the ultra-low interest rates. Consumer credit again decreased in December (-1.1% yoy).

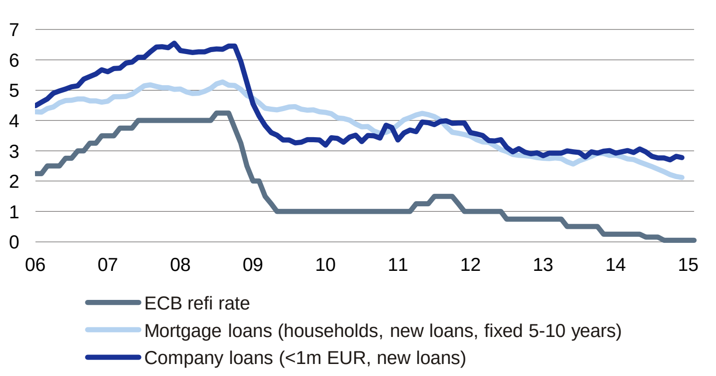
Lending to the private sector (% yoy)



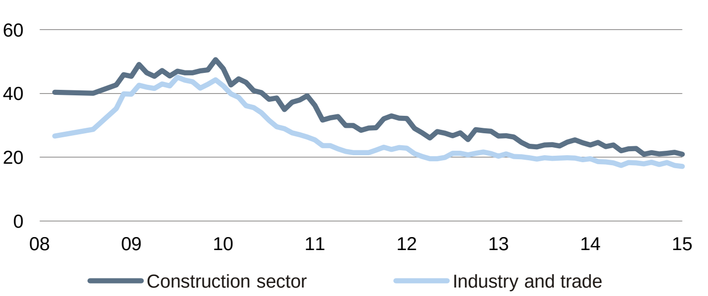
Loans to households (% yoy)



Interest rates (%)



Companies' view on access to credit



Credit constraints: Percentage of companies reporting restrictive access to credit. Higher values indicate more restrictive access to credit from companies' perspective

Sources: ECB, ifo, Deutsche Bank Research

Chartbook – Public finances

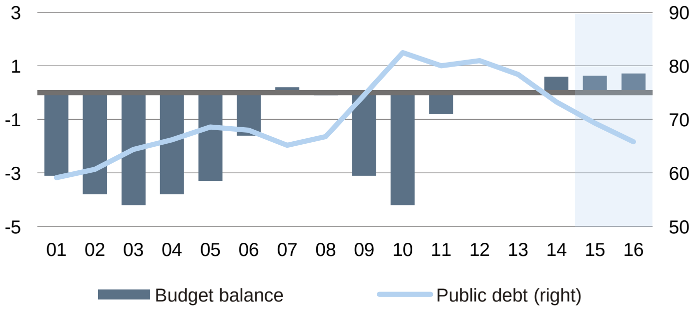
— As in 2013 (0.1%), the general government budget closed with a small surplus in 2014 (0.6%). The budget situation is unlikely to change appreciably in 2015 and should see a comparable surplus again at year-end. This will be driven mainly by the still good revenue prospects in view of the favourable economic outlook. The robust growth of revenues will probably suffice in the current year to compensate for a number of measures representing fiscal burdens, such as the introduction not only of the nationwide minimum wage but also retirement at 63 and higher pensions for mothers whose children were born before 1992. The financial buffer provided by the social security system will continue to shrink, though, owing to the broader spectrum of benefits offered. One of the causes of the steadily higher revenue volume is that for several years there has basically been no change in the income tax scale. This heightens the fiscal drag of what is known in Germany as "cold progression". Changes in this area are currently a controversial issue. As the report on the minimum subsistence level has been now tabled it is necessary to adjust the personal tax allowance anyway.

— One year earlier than anticipated, the German government has already been able to close 2014 with a balanced budget. The budget is forecast to be in equilibrium again in 2015. The chances of this happening are good as long as there are no major unforeseen extra burdens on the budget – as would be the case, for instance, in the event of a potential renewed haircut on Greek debt. The municipalities and social security closed 2014 in the black again, too – however, the surplus was much smaller than in 2013. Also the aggregate Länder budgets showed a small surplus for the first time in quite a while. Within the Länder group – as among the municipalities – the situation remains very mixed, however. A host of Länder are deep in the red, while others report surpluses and can reduce their debt. In 2014, not only the general budget but also the Federation budget was structurally balanced for the first time in a long time. This means that since 2012 these have already complied continuously with the regulations for the debt brake that will apply in full force from 2016.

— Public debt (under the Maastricht definition) equalled only 74.8% of GDP at the end of Q3 2014 (down from 76.9% in Q4 2013). Over the next few years sovereign debt is likely to steadily decrease further on a continuation of the economic dynamics. The fact that the bad banks continue to run down their portfolios will alone cut debt by an additional roughly 0.5% of GDP p.a. This suggests that the debt ratio could slip back under 70% of GDP for the first time since 2008 as early as this year.

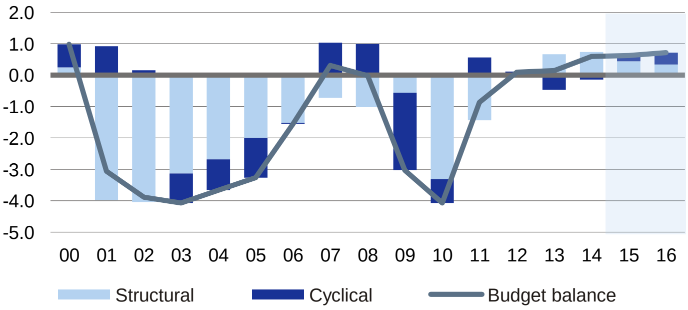
Public debt and budget balance

General government, as % of GDP,



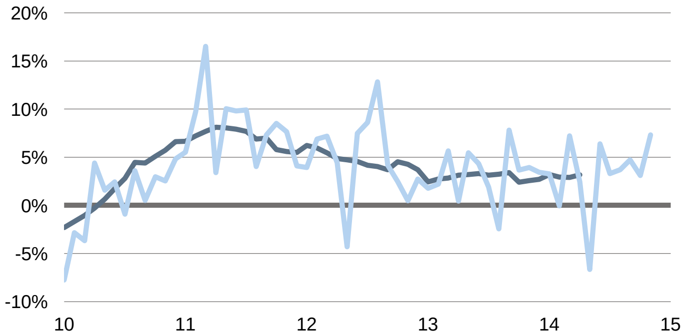
Budget balance

General government, % of GDP



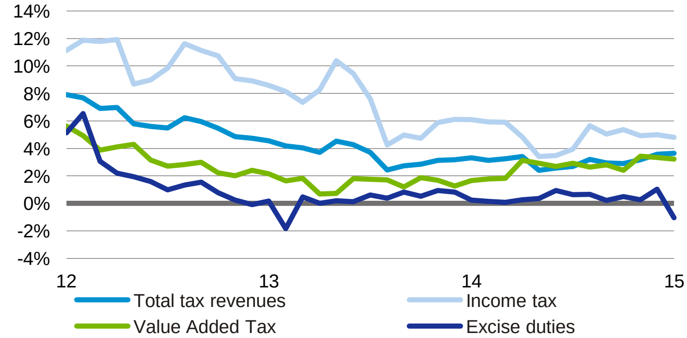
Tax revenues

Monthly data, yoy and yoy 12 months moving average



Development of important taxes

Change yoy, 12 months moving average



Sources: Deutsche Bank Research, European Commission, Bundesbank

Germany: Events of economic-, fiscal- and euro-politics

Date	Event	Remarks
5 Mar	ECB Governing Council meeting in Cyprus	The ECB will begin purchasing euro-denominated bonds issued by euro area governments, agencies and European institutions from March onwards.
9/10 Mar	Eurogroup and ECOFIN, Brussels	Fiscal surveillance: EDP implications of the Commission winter forecast, enhanced monitoring under the Macroeconomic Imbalances Procedure (MIP), Cyprus – 6th review, others.
19/20 Mar	European Council, Brussels	Debates on an Energy Union, on relations with Russia and the situation in Ukraine, preparations of the Eastern Partnership Summit in Riga, conclusion of the first phase of the 2015 European Semester.
15 Apr	ECB Governing Council meeting, press conference	Review of the monetary policy stance.
17 to 19 Apr	G20 Finance Ministers and Central Bank Governors Meeting and spring meeting of IMF and World Bank, Washington	Debates on the global economy, and the world's financial markets.

Source: Deutsche Bank Research

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Germany: Data calendar

Date	Time	Data	Reporting period	DB forecast	Last value
3 Mar 2015	8:00	Retail sales (Index, sa), pch mom	January	-0.5	0.6
5 Mar 2015	8:00	New orders manufacturing (Index, sa), pch mom	January	-2.5	4.2
6 Mar 2015	8:00	Industrial production (Index, sa), pch mom	January	1.0	0.1
9 Mar 2015	8:00	Trade balance (EUR bn, sa)	January	23.2	22.0
9 Mar 2015	8:00	Merchandise exports (EUR bn, sa), pch mom (yoy)	January	1.9 (6.8)	3.9 (7.3)
9 Mar 2015	8:00	Merchandise imports (EUR bn, sa), pch mom (yoy)	January	0.9 (2.0)	-0.2 (3.2)
24 Mar 2015	9:30	Manufacturing PMI (Flash)	March	51.1	50.9
24 Mar 2015	9:30	Services PMI (Flash)	March	54.5	55.5
25 Mar 2015	10:30	ifo business climate (Index, sa)	March	107.0	106.8
31 Mar 2015	10:00	Unemployment rate (%, sa)	March	6.5	6.5
27 Mar 2015	8:00	Import prices (Index, sa) pch mom (yoy)	February	1.1 (-3.3)	-0.8 (-4.4)
30 Mar 2015	14:00	Consumer prices preliminary (Index, sa), pch mom (yoy)	March	0.5 (0.4)	0.9 (0.1)
13 May 2015	8:00	Real GDP (Index, sa), % qoq	Q1 2015	0.5	0.7

Sources: Deutsche Bank Research, Federal Statistical Office, Federal Employment Agency, ifo, Markit

Financial forecasts

	US	JP	EMU	GB	CH	SE	DK	NO	PL	HU	CZ
Key interest rate, %											
Current	0.125	0.10	0.05	0.50	-1.25	-0.10	0.05	1.25	2.00	2.10	0.05
Mar 15	0.250	0.10	0.05	0.50	-0.75	-0.10	0.05	1.25	1.75	1.85	0.05
Jun 15	0.500	0.10	0.05	0.50	-0.75	-0.10	0.05	1.25	1.50	1.85	0.05
Dec 15	1.000	0.10	0.05	0.50	-0.75	-0.10	0.05	1.25	1.50	1.85	0.05
3M interest rates, %											
Current	0.35	0.20	0.04	0.56							
Mar 15	0.35	0.15	0.00	0.58							
Jun 15	0.75	0.15	0.00	0.59							
Dec 15	1.35	0.15	-0.10	0.60							
10Y government bonds yields, %											
Current	1.96	0.34	0.33	1.80	0.00	0.00	0.00	0.00			
Mar 15	1.85	0.40	0.30	1.50	0.00	0.00	0.00	0.00			
Jun 15	2.50	0.45	0.40	1.70	0.00	0.00	0.00	0.00			
Dec 15	2.65	0.60	0.40	2.25	0.00	0.00	0.00	0.00			
Exchange rates											
	EUR/USD	USD/JPY	EUR/GBP	GBP/USD	EUR/CHF	EUR/SEK	EUR/DKK	EUR/NOK	EUR/PLN	EUR/HUF	EUR/CZK
Current	1.12	119.26	0.73	0.65	1.07	9.41	7.47	8.57	4.16	303.03	27.43
Mar 15	1.11	119.00	0.73	1.52	1.05	9.20	7.46	8.90	4.16	310.00	27.50
Jun 15	1.09	121.00	0.74	1.47	1.07	9.00	7.46	9.00	4.13	310.50	27.50
Dec 15	1.05	125.00	0.77	1.36	1.10	8.90	7.46	8.90	4.08	315.00	27.50

Sources: Bloomberg, Deutsche Bank

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German data monitor

	Q1 2014	Q2 2014	Q3 2014	Q4 2014	Q1 2015	Sep 2014	Oct 2014	Nov 2014	Dec 2014	Jan 2015	Feb 2015
Business surveys and output											
Aggregate											
Ifo business climate	110.9	110.1	106.6	104.5		105.4	103.4	104.6	105.5	106.7	106.8
Ifo business expectations	107.5	105.6	101.8	100.1		100.2	98.9	100.2	101.3	102.0	102.5
PMI composite	55.4	55.2	54.5	52.5		54.1	53.9	51.7	52.0	53.5	54.3
Industry											
Ifo manufacturing	107.0	106.3	102.7	99.7		101.4	98.5	99.4	101.1	102.2	102.3
Headline IP (% pop)	1.1	-1.0	-0.3	0.5		1.0	0.6	0.1	0.1		
Orders (% pop)	0.0	-0.2	0.2	1.9		1.1	2.9	-2.4	4.2		
Capacity Utilisation	84.0	83.9	83.8	84.2	84.6						
Construction											
Output (% pop)	5.7	-4.7	-0.1	1.1		1.5	-0.1	0.7	0.7		
Orders (% pop)	1.8	-5.2	-2.4	-0.4		-0.8	0.9	0.6	1.6		
Ifo construction	122.8	119.9	120.3	120.3		120.9	120.8	120.7	119.5	119.2	119.1
Consumer demand											
EC consumer survey	0.3	4.3	1.0	-1.2		-1.1	-0.7	-1.6	-1.4	0.0	-0.1
Retail sales (% pop)	1.9	-0.3	-0.1	1.5		-1.7	2.0	0.5	0.6		
New car reg. (% yoy)	2.8	-0.3	4.1	2.7		5.2	3.7	-1.8	6.7	2.6	
Foreign sector											
Foreign orders (% pop)	-1.4	0.3	1.9	1.9		4.0	0.6	-0.9	4.8		
Exports (% pop)	-0.1	0.5	2.7	1.9		5.1	1.4	-3.6	3.9		
Imports (% pop)	0.2	0.0	0.8	1.3		4.8	-1.8	1.2	-0.2		
Net trade (sa EUR bn)	53.5	54.7	60.4	62.9		19.9	22.7	18.2	22.0		
Labour market											
Unemployment rate (%)	6.8	6.7	6.7	6.6		6.7	6.6	6.6	6.5	6.5	6.5
Change in unemployment (k)	-41.0	-19.0	1.7	-38.0		8.0	-24.0	-16.0	-26.0	-10.0	-20.0
Employment (% yoy)	0.7	0.9	0.9	1.0		0.9	1.0	1.0	1.0	1.0	
Ifo employment barometer	107.6	106.8	106.5	106.3		106.1	107.1	105.2	106.7	108.1	106.8
Prices, wages and costs											
Prices											
Harmonised CPI (% yoy)	1.0	0.9	0.8	0.4		0.8	0.7	0.5	0.1	-0.5	-0.1
Core HICP (% yoy)	1.1	1.1	1.2	1.1		1.2	1.1	0.9	1.2	0.8	
Harmonised PPI (% yoy)	-1.0	-0.8	-0.8	-1.2		-1.0	-1.0	-0.9	-1.7	-2.2	
Commodities, ex. Energy (% yoy)	-11.1	-4.9	-1.8	0.9		-1.1	0.9	1.7	0.1	2.3	
Oil price (USD)	108.2	109.7	102.0	76.4		97.4	87.3	78.8	63.1		
Inflation expectations											
EC household survey	22.0	16.9	13.4	8.6		10.0	11.1	8.5	6.2	0.5	-0.7
EC industrial survey	5.6	2.3	4.2	2.1		5.2	4.7	3.2	-1.5	-1.2	-0.1
Unit labour cost (% yoy)											
Unit labour cost	0.8	2.0	2.0	1.7							
Compensation	2.8	2.5	2.5	2.3							
Hourly labour costs	0.8	2.3	2.1	1.6							
Money (% yoy)											
M3	3.8	4.5	4.7	4.7		4.7	4.0	5.1	4.7	5.9	
M3 trend (3m cma)						4.5	4.6	4.6			
Credit - private	-3.6	-3.5	1.4	1.7		1.4	1.2	1.5	1.7		
Credit - public	-1.5	9.7	5.9	12.6		5.9	5.1	3.6	12.6		

% pop = % change this period over previous period.
Sources: Deutsche Bundesbank, European Commission, Eurostat, Federal Employment Agency, German Federal Statistical Office, HWWI, ifo, Markit

Deutsche Bank
Research

Focus Germany

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