Germany: Economic Chartbook

Team Economic Research Frankfurt

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GDP now expected to fall by -0.5% in 2023, 2024 cut to 0.3%

German GDP forecast lowered to -0.5% in 2023 and 0.3% in 2024. After the technical recession in winter 22/23, the H1 recovery disappointed, as consumers are becoming more cautious. Given the weak PMIs, ifo and other high-frequency indicators, a renewed GDP qoq contraction in Q3 is now our baseline call.

Various growth drivers are sputtering simultaneously. Recent downward revisions to Chinese GDP forecasts and a US recession still expected in Q4 promise little external support in H2 and into next year. The domestic economy is being burdened by higher financing costs and weak consumer confidence weighing on their propensity to buy, despite stabilizing incomes.

Data on private household finance suggest that liquid funds have shifted into capital markets, rather than being spent.

The German labor market is losing momentum. Leading indicators hint at cracks, but qualified labor is still in high demand. Wage increases in 2023 dominated by strong one-off payments, while pay scale rises will largely start in 2024.

Headline inflation is set to fall considerably in 2023/24. By contrast, core inflation is likely to remain relatively sticky. Medium-term inflation expectations are still elevated and have ticked up again lately, although selling price expectations have fallen below their long-term average.

Corporate lending substantially slowing. Higher interest rates and a low propensity to invest have put the breaks on loan demand.

German green trade surplus. The global export market for low-carbon-technology products is growing faster than the export market for goods overall. EVs, hybrid cars, measuring instruments and machines drive Germany’s green trade surplus.

Fiscal budget impact from energy price shock might be less severe. But debt interest payments are set to increase strongly.

German office market. Infrastructure bottlenecks could be an underappreciated obstacle for office demand, especially in A cities.

An historic flashback? We revisit the challenges Germany was facing when the Economist called it the ‘sick man of the euro’ and which policy measures transformed the country into an economic superstar a decade later.

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Key Economic Forecasts

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

	2021	2022	2023F	2024F	2022 Q1	2022 Q2	2022 Q3	2022 Q4	2023 Q1	2023 Q2	2023 Q3F	2023 Q4F
Real GDP	3.2	1.8	-0.5	0.3	1.0	-0.1	0.4	-0.4	-0.1	0.0	-0.3	0.0
Private consumption	1.5	3.9	-0.8	1.5	0.6	0.2	0.7	-1.0	-0.3	0.0	0.1	0.3
Gov't expenditure	3.1	1.6	-1.6	1.9	1.4	-0.1	-1.1	-0.2	-1.9	0.1	1.0	1.0
Fixed investment	-0.2	0.1	0.6	-0.4	2.2	-1.6	1.0	-1.3	1.7	0.4	-0.9	-0.4
Investment in M&E	2.8	4.0	3.8	1.2	1.9	1.6	4.2	-1.5	2.1	0.6	-0.5	0.0
Construction	-2.6	-1.8	-1.3	-2.6	3.3	-3.9	-0.6	-2.0	2.7	0.2	-1.5	-1.0
Inventories, pp	0.9	0.7	-0.1	-0.2	0.1	0.7	0.4	0.2	-0.8	0.4	-0.2	-0.2
Exports	9.7	3.3	-0.9	1.1	-0.1	0.9	1.0	-1.1	0.4	-1.1	0.3	0.5
Imports	8.9	6.6	-1.5	2.3	0.1	2.4	1.8	-1.7	-1.5	0.0	0.7	0.8
Net exports, pp	0.9	-1.2	0.2	-0.5	-0.1	-0.6	-0.3	0.2	0.9	-0.6	-0.2	-0.1
Consumer prices (CPI)*	3.1	6.9	6.1	2.3								
Unemployment rate, %	5.7	5.3	5.6	5.5								
Industrial production**	4.8	-0.3	1.0	0.5								
Budget balance, % GDP	-3.6	-2.5	-2.1	-1.4								
Public debt, % GDP	69.3	66.3	65.9	65.5								
Balance on current account, %	7.7	4.2	5.0	4.8								
Balance on current account, EUR	265	115.0	205	205								

* This can lead to discrepancies to other DB publications which report HICP. ** Manufacturing (NACE C).

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

Germany: Data release calendar

Date	Time	Data	Reporting period	DB forecast	Last
4 Sep 2023	8:00	Trade balance (EUR bn, sa)	July	19.5	18.7
4 Sep 2023	8:00	Merchandise exports (% mom, sa)	July	1.0	0.4
4 Sep 2023	8:00	Merchandise imports (% mom, sa)	July	0.5	-3.2
6 Sep 2023	8:00	New orders manufacturing (% mom, sa)	July	-3.0	7.0
7 Sep 2023	8:00	Industrial production (% mom, sa)	July	0.5	-1.2
22 Sep 2023	9:30	Manufacturing PMI (Flash)	September	40.0	39.1
22 Sep 2023	9:30	Services PMI (Flash)	September	48.0	47.3
25 Sep 2023	10:00	ifo business climate (Index, sa)	September	86.5	85.7
28 Sep 2023	14:00	Consumer prices preliminary (% yoy, nsa)	September	4.4	6.1
28 Sep 2023	14:00	Consumer prices preliminary (% mom, nsa)	September	0.1	0.3
28 Sep 2023	14:00	Core consumer prices (% yoy, nsa)	September	4.6	5.5
28 Sep 2023	14:00	Core consumer prices (% mom, nsa)	September	0.3	0.2
29 Sep 2023	8:00	Retail sales (% mom, sa)*	August	0.8	-0.8
29 Sep 2023	9:55	Unemployment rate (%, sa)	September	5.7	5.7

*An earlier data release may be possible due to the Federal Statistical Office.

Sources: Deutsche Bank Research, Federal Statistical Office, Federal Employment Agency, ifo, S&P Global, HCOB

2023 Event calendar: DE/EU/EA

September 14	ECB Governing Council: Monetary policy meeting
October 8	Regional elections in Bavaria
October 8	Regional elections in Hesse
October 26	ECB Governing Council: Monetary policy meeting
October 26/27	European Council meeting
December 14	ECB Governing Council: Monetary policy meeting
December 14/15	European Council meeting

Source: Deutsche Bank Research

Global economy remains sluggish. China's recovery is struggling, US outlook is clouded, despite current resilience

- Tailwinds from the post-Covid catch-up and the avoidance of an even more severe energy crisis may have faded. Geopolitical risks are a concern.
- In China, the real estate sector and weak domestic demand are slowing the economy. The weakening of the outlook also suggests less impetus for the global economy.
- In the US, Fed's tightening is likely to induce a mild recession by Q4 2023. But for now, the economy remains surprisingly robust.
- Eurozone GDP is expected to stagnate during the coming quarters as monetary tightening impacts economies. Downside risks are accumulating.
- Above-target (core) inflation remains key concern of Fed and ECB. Both should have reached their target rates (Fed: 5.375%, ECB: 3.75% (deposit rate)) by now, but this remains a very close call.

Economic growth

Real GDP, % yoy

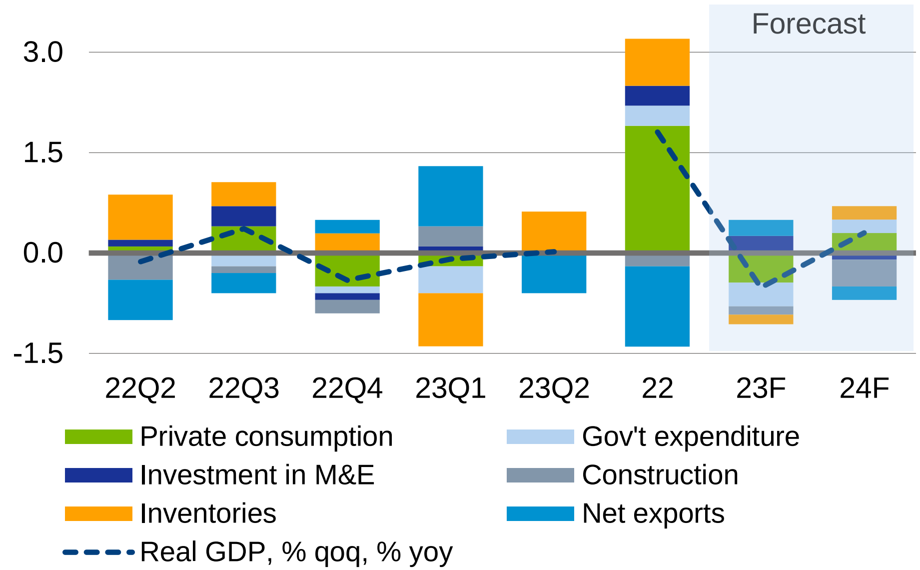
	2021	2022	2023F	2024F
US	5.9	2.1	2.1	0.0
Japan	2.3	1.0	2.2	0.7
Euroland	5.4	3.4	0.5	0.5
Germany	3.2	1.8	-0.5	0.3
France	6.4	2.5	0.6	0.2
Italy	7.0	3.8	1.1	0.4
Spain	5.5	5.5	2.0	0.9
Netherlands	6.2	4.3	1.0	1.2
Greece	8.4	5.9	2.4	1.5
Portugal	5.5	6.7	1.4	1.7
Ireland	15.1	9.4	5.6	4.8
UK	7.6	4.1	0.3	0.4
Asia (ex Japan)	7.4	4.1	4.8	4.8
China	8.4	3.0	5.0	4.7
India	8.9	6.7	6.3	6.0
Eastern Europe	5.9	2.9	2.6	3.2
Latin America (ex Venezuela)	7.3	3.8	1.8	1.5
World	**6.4**	**3.3**	**2.9**	**2.6**

Sources: IMF, Bloomberg Finance LP, Deutsche Bank Research

Outlook update: German GDP likely to shrink by 0.5% in 2023 and to grow by only 0.3% in 2024

German GDP and components: Private consumption stabilized in Q2

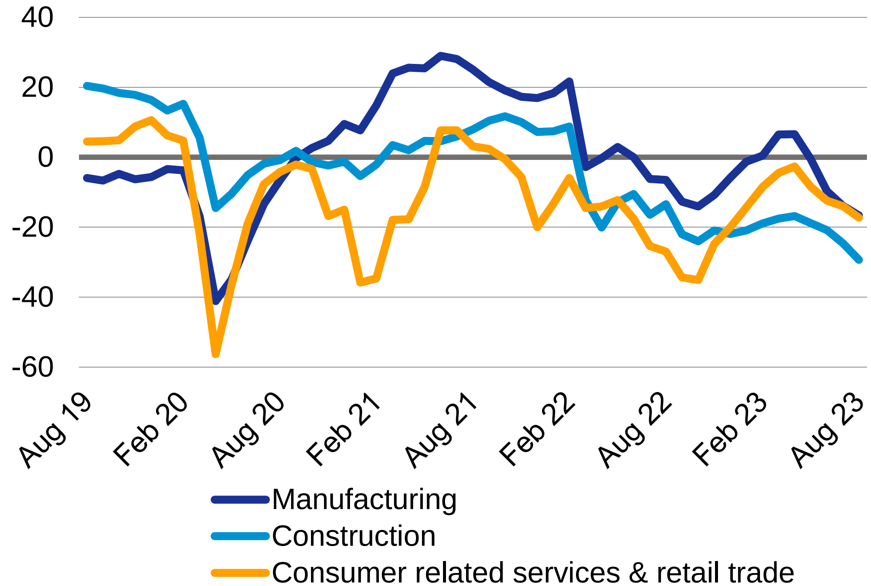
Contributions to real GDP growth, qoq, yoy, pp



Sources: Federal Statistical Office, Deutsche Bank Research

ifo Business Climate signals widespread growth pessimism

Balances



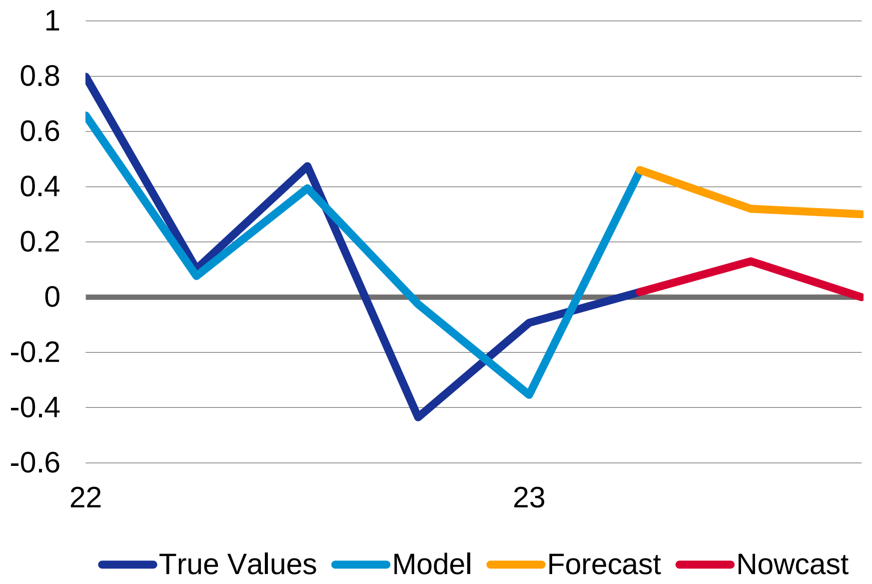
Source: ifo

- After only stagnating qoq in Q2, GDP is expected to shrink by some 0.3% in Q3, given the recent setback to sentiment indicators and higher frequency activity data. Growth in Q4 is likely to remain flat.
- Towards year-end, a recovery is likely to be held back by the expected US recession, weaker external demand in general as well as restrained domestic consumption and, above all, the impact of tighter monetary policy.
- Private consumption is likely to pick up more strongly in 2024, once inflation has fallen more significantly and the already strong wage settlements are also reflected in noticeable real income gains.

Nowcasting German GDP: H2 predictions have deteriorated significantly with the emergence of negative data in Q3

GDP Forecast vs. Nowcast 2023

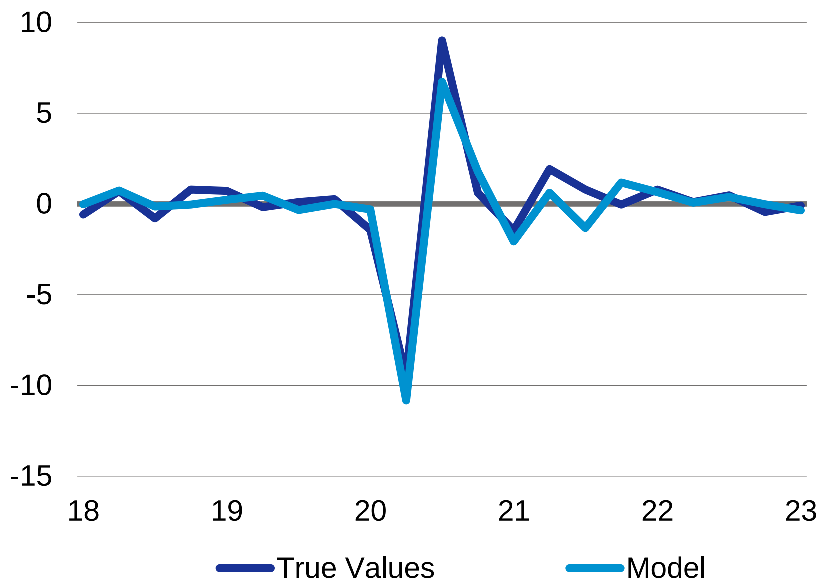
growth rate, % qoq



Source: Deutsche Bank Research

In-sample model performance

growth rate, qoq in percent



Source: Deutsche Bank Research

- Taking into account the data available so far, our new GDP Nowcast now signals a meagre 0.1% qoq in Q3 (Q4 almost flat), while the previous forecast based on Q2 data still suggested that +0.4% was likely for Q3.
- Our new Nowcast model complements the battery of bridge models used for the short- and medium-term GDP forecast. It expands the input database, especially with a view to higher-frequency data.
- By allowing the impact of the factors to be time-varying (i.e., dynamic), the approach provides more flexibility to pick up contemporaneous information that influences both forecasts and nowcasts.

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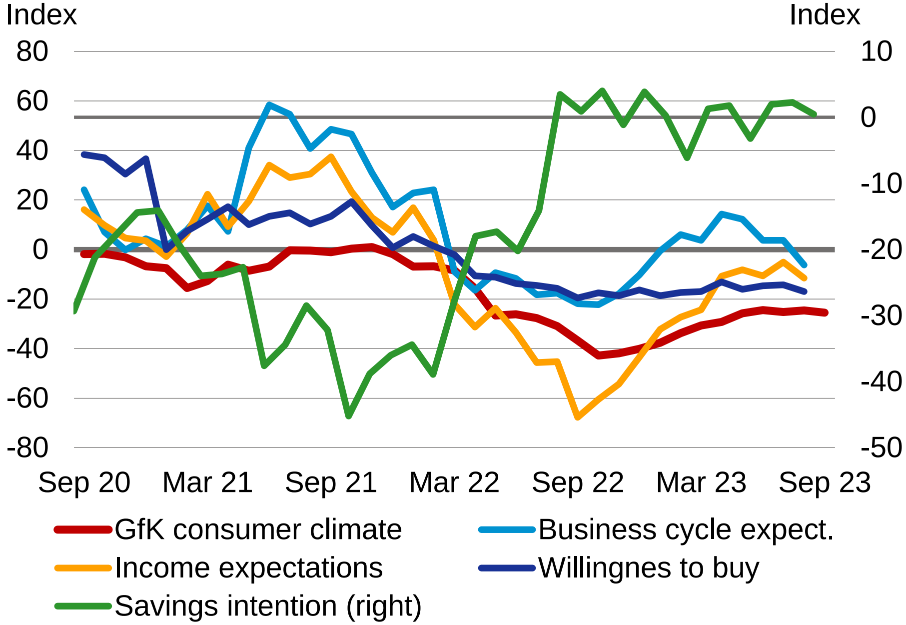
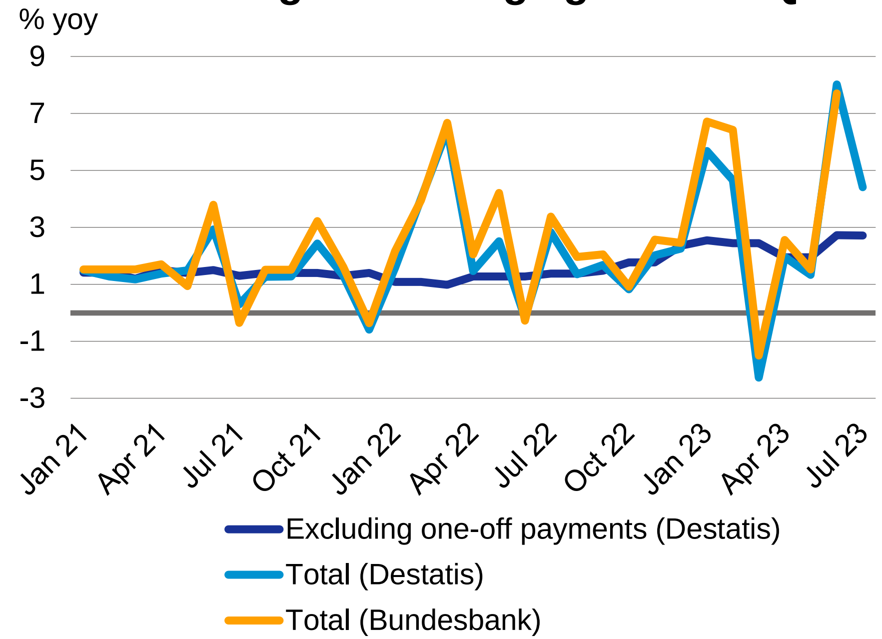
Consumers are not in buying mood again, despite strong one-off payments supporting real incomes

GfK consumer sentiment remains subdued in H2



Source: GfK

Strong one-offs in public services and manufacturing drove wage growth in Q2



Sources: Federal Statistical Office, Deutsche Bundesbank

- The propensity to buy among private households is still subdued. Subcomponents of the latest GfK consumer climate index signal rising economic pessimism and pre-cautionary saving.
- Incomes of many households have already been supported, among other things, by tax- and levy-exempted inflation-related one-off payments or by pension increases (July, West: 4.39% East: 5.86%).
- In order to revive private consumption, it will probably need lower inflation, permanent wage increases kicking in (many industries already agreed for 2024), and a better macro outlook.

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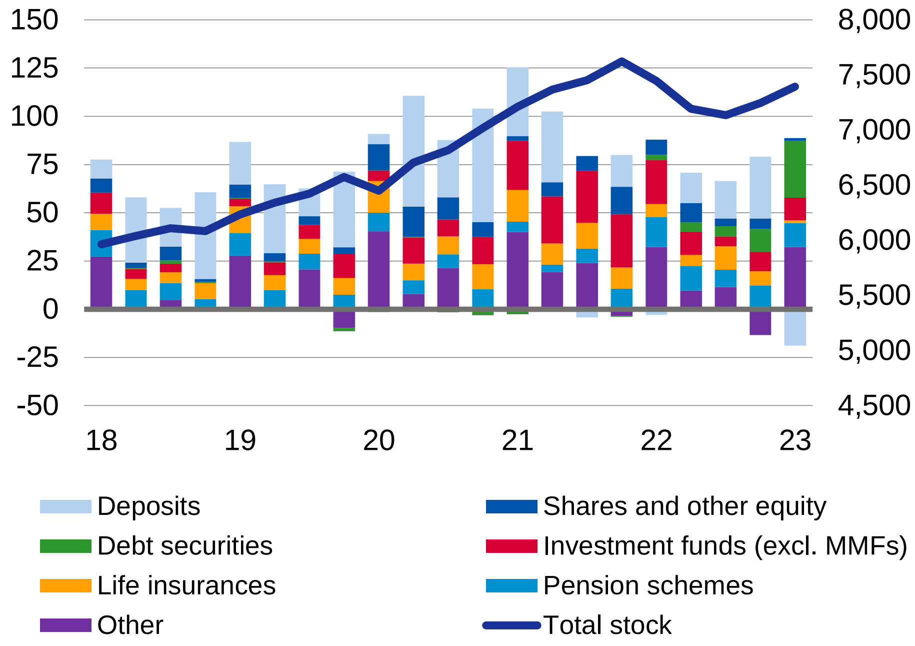
Private households go to the capital markets and keep bank credit almost flat

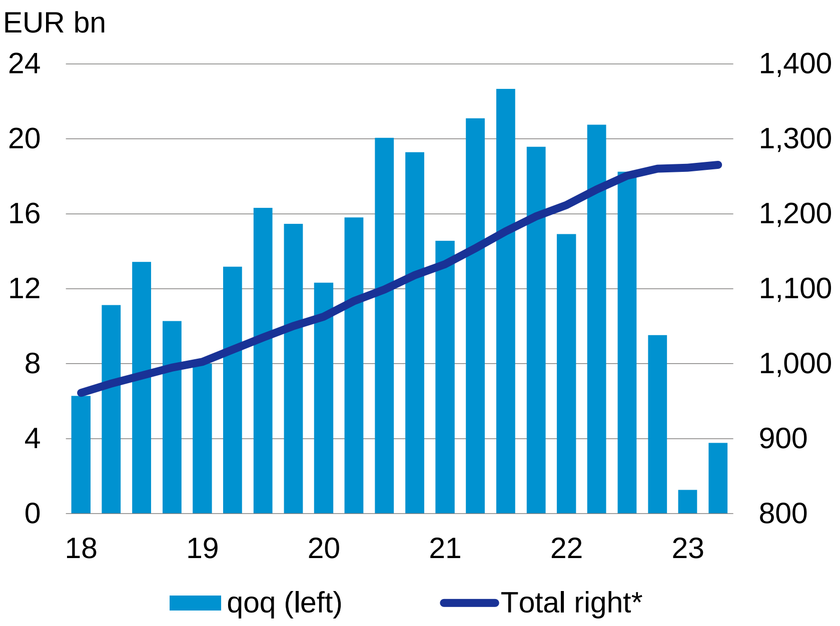
Strong investments in capital markets – record deposit outflow

Financial assets of households, EUR bn; net flows (left), stock (right)



Sources: ECB, Deutsche Bank Research

Mortgage market reaching bottom



*includes significant reclassification in Q3 18.

Sources: Deutsche Bundesbank, Deutsche Bank Research

- Probably meagre deposit increases going forward, with strong shifts from sight deposits into term deposits.
- Sizable investments in other financial assets, but still real losses in financial wealth.
- Low but positive mortgage growth expected as mortgage rates will likely stabilize.

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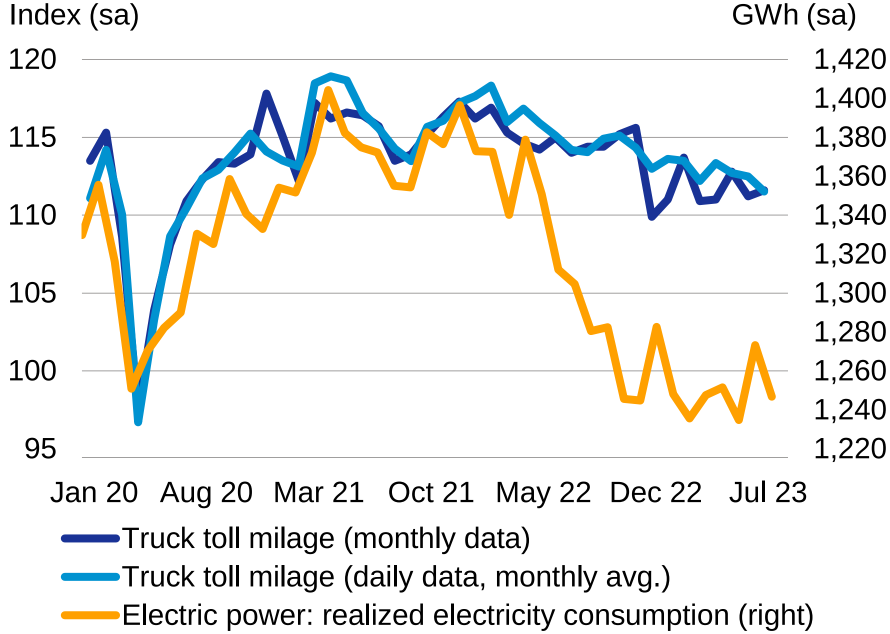
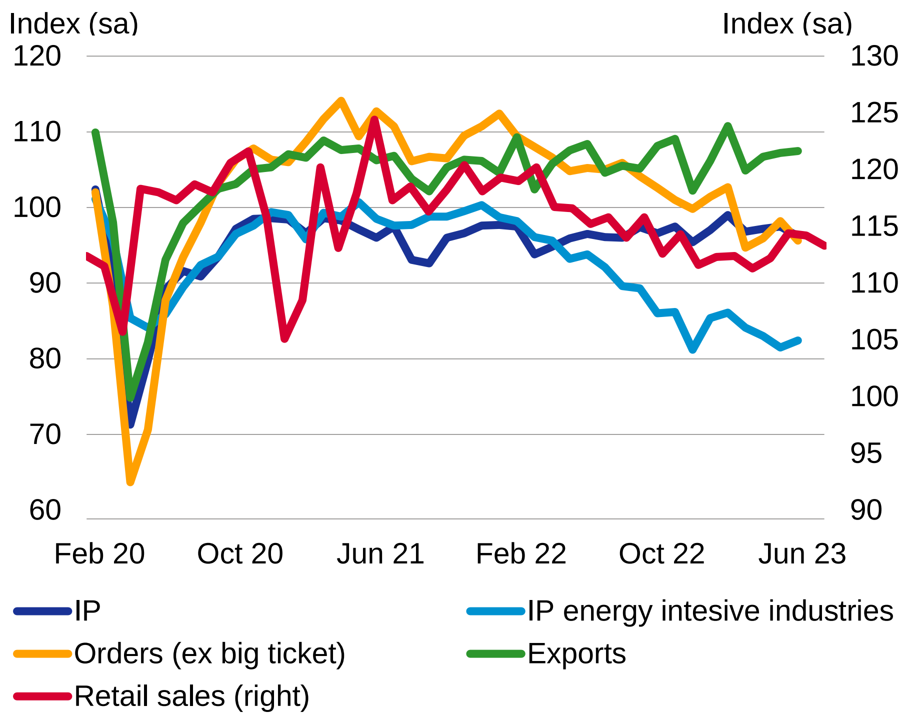
Hard data stuck in a rut until mid-summer, leading activity indicators weakened into Q3

High-frequency data signal a weak start into Q3



Sources: Federal Statistical Office, Federal Network Agency, Deutsche Bundesbank

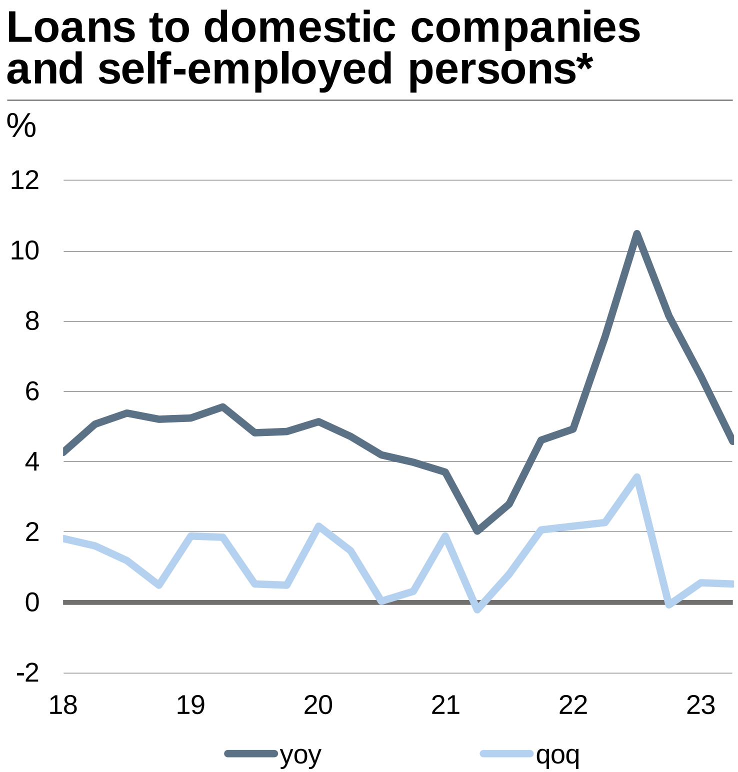
German hard data



Source: Federal Statistical Office

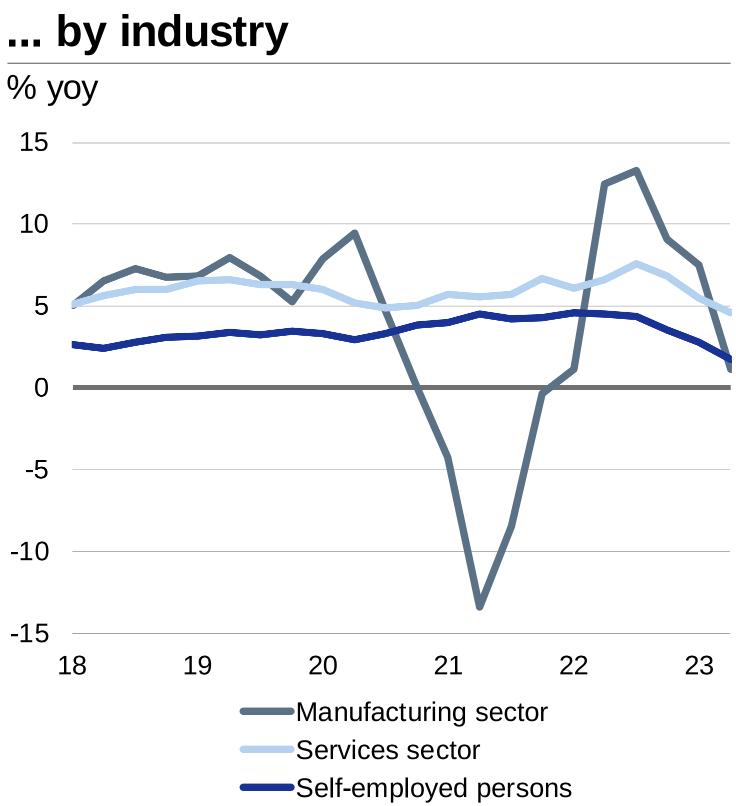
- While there was no noticeable recovery in German hard data until mid-summer, most recent leading indicators are even pointing to a further weakening.
- For various industries, the cost of energy is still a headwind, even if prices have meanwhile moved well away from their peaks again.
- Good news? Sub-components of the manufacturing PMI signal a slowing decline in input prices in August. Given the weakening global economic activity, remaining supply bottlenecks are likely to ease further.

Lending slowing substantially due to weak demand in the wake of surging interest rates & firms' low propensity to invest



* excl. other financial institutions

Sources: Bundesbank, Deutsche Bank Research



Sources: Bundesbank, Deutsche Bank Research

- Loans to companies and self-employed persons in Germany rose again only slightly in Q2, by EUR 8.3 bn or 0.5% compared to March. In the euro area, volumes even stagnated.
- Slowdown driven by demand rather than supply: tightening of credit standards is coming to an end, but demand continues to slump as firms are cutting back on investment & have to stomach the much higher rates.

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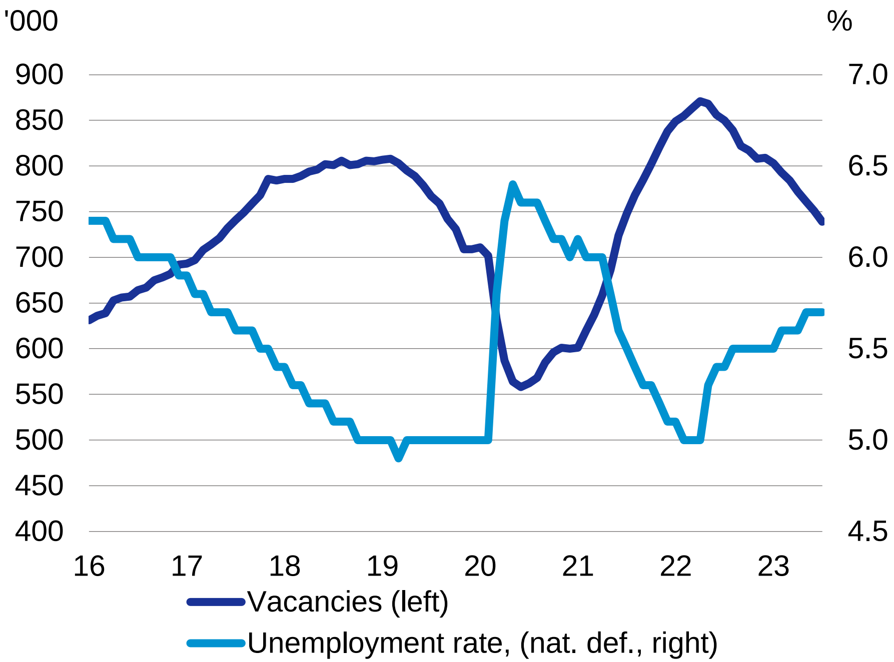
German labor market losing momentum, leading indicators hint at cracks, but qualified labor is still in high demand

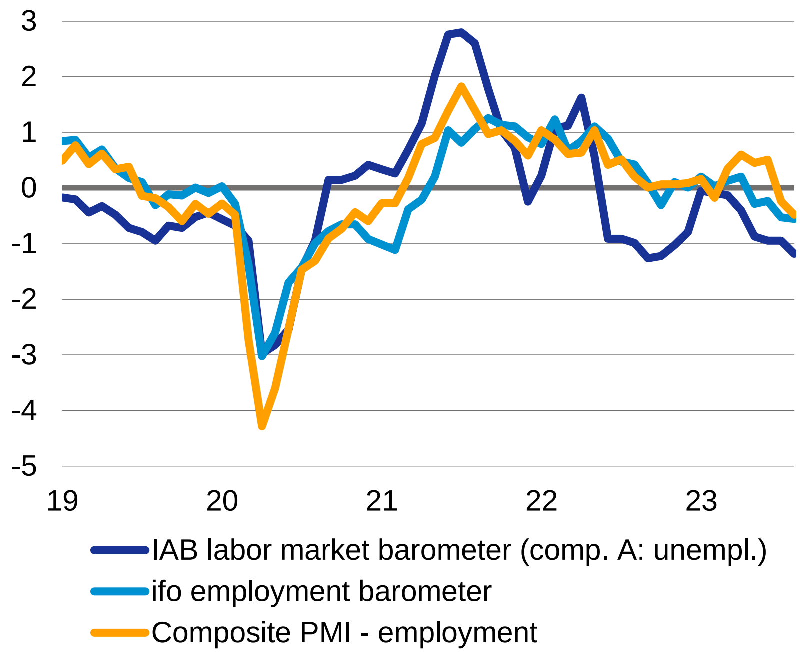
Labor market loses momentum, special factor Ukrainian refugees



Source: Federal Employment Agency

Labor market indicators

Standardised values



Sources: ifo, IAB, S&P Global, HCOB, Federal Employment Agency

- The weak economy is leaving its mark on the labor market, particularly visible in the decline in job vacancies, but unemployment has also increased recently, even adjusted for the impact of Ukrainian refugees.
- Growth in employment s.t. social security contributions (May: 34.8 m) and in total employment (Jun: 45.9 m) appears to have plateaued at their respective highs in a seasonally adjusted comparison with the previous month.
- Leading labor market indicators point to rising unemployment and at least only stagnant employment.

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Wage increases in 2023 dominated by strong one-off payments, while pay scale rises will largely start in 2024

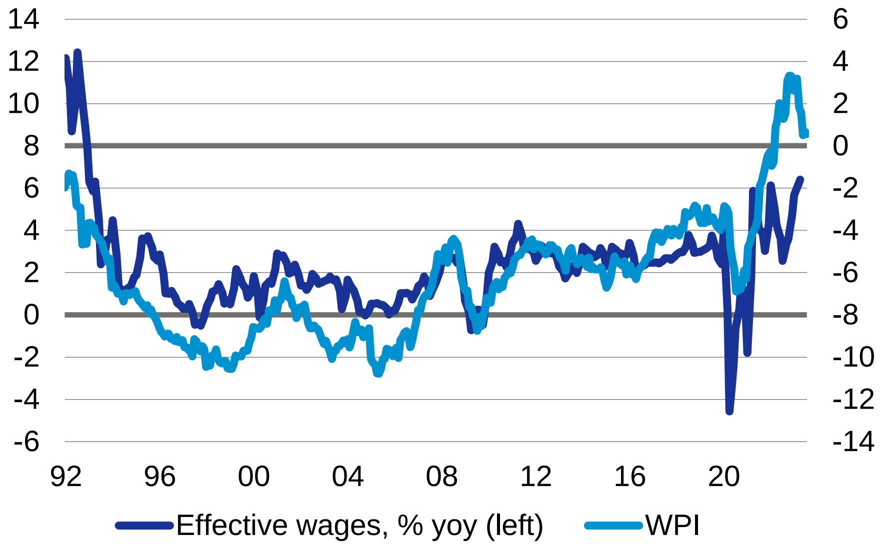
Wage negotiations in selected* sectors

Sector	Expiry date	Employees
Retail trade (Hesse)	underway	592,700
Retail trade (North Rhine-Westphalia etc.)	underway	1,583,900
Wholesale and foreign trade (North Rhine-Westphalia etc.)	underway	1,175,300
Retail trade (Saxony-Anhalt, Thuringia, Saxony)	underway	212,200
Retail trade (Berlin, Brandenburg)	underway	234,400
Civil service (federal states, excl. Hesse)	Sep 30	938,800
Wood and plastics processing (various regions)	Nov 30	178,900

*Negotiations for more than 100,000 employees

Sources: WSI-Tarifarchiv, Deutsche Bank Research

German wage pressure index (WPI) eased recently



Sources: Deutsche Bundesbank, Deutsche Bank Research

- So far, the government's offer to exempt one-off payments of up to EUR 3,000 from taxes and social security contributions has helped to reach relatively moderate permanent wage increases for the 2023/24 period.
- Protracted bargaining rounds and negotiations in the public sector of the German federal states (Oct.) are likely to affect the pattern of respective growth rates of collectively agreed wages excluding one-off payments and effective wages for 2023 and 2024.
- Collectively agreed wages ex one-offs are likely to rise 4.5% in 2023 and a good 5.5.% in 2024. Not least because inflation compensation one-offs (also outside regular pay structure), effective/total earnings are likely to rise by around 6% in 2023 and a good 5% in 2024.

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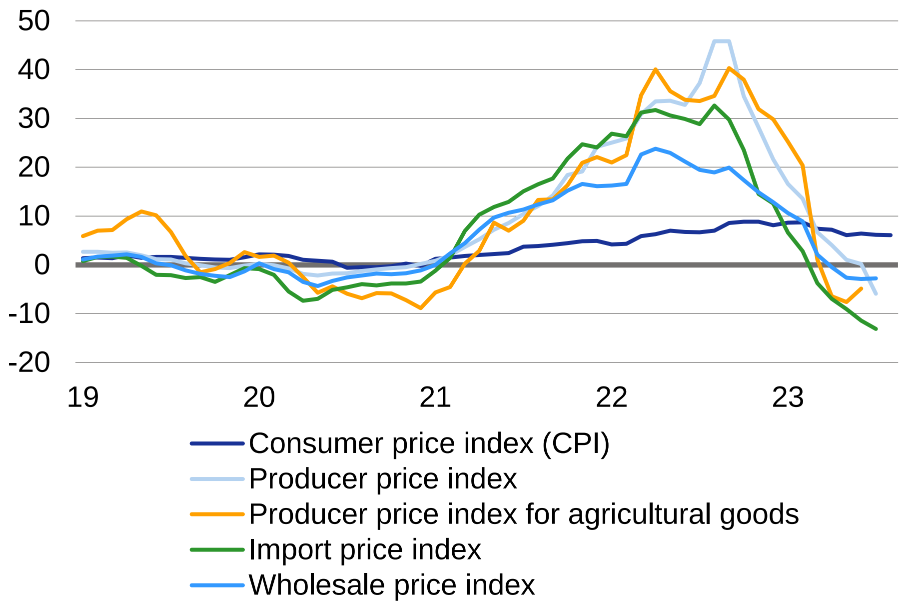
Headline inflation is set to fall considerably in 2023/24 but core inflation might remain relatively sticky

Price developments at the upstream level

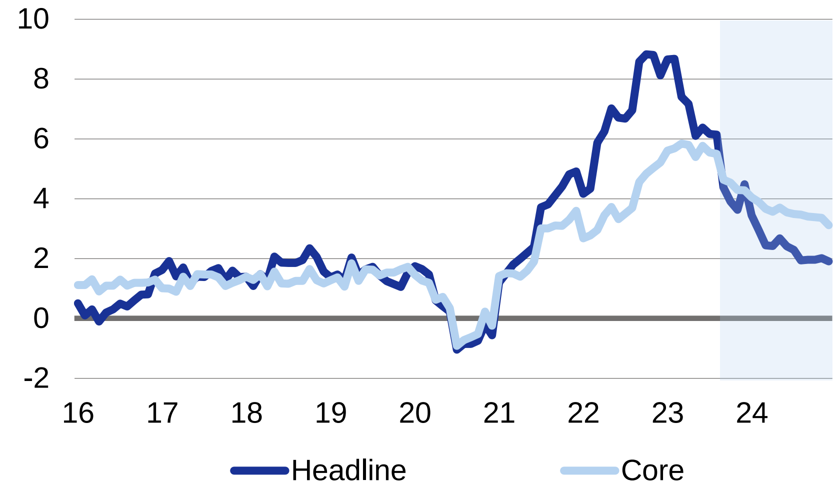
% yoy



Sources: WEFA, Federal Statistical Office,
Deutsche Bank Research

Headline inflation is set to fall considerably in 2023/24

% yoy



Sources: WEFA, Federal Statistical Office,
Deutsche Bank Research

- Owing to disinflationary effects from energy, food, and core goods prices, we project the CPI inflation rate to fall substantially further over the course of 2023/24, possibly easing to a level of around 4 ½% by the end of this year and undercutting the 2%-mark by Dec-2024.
- Contrary, core inflation might fall much more slowly, ending 2023 at a still elevated level of +4%. Because of the lagged effects from higher wages, core inflation might still stand above the 3% mark by Dec-24.

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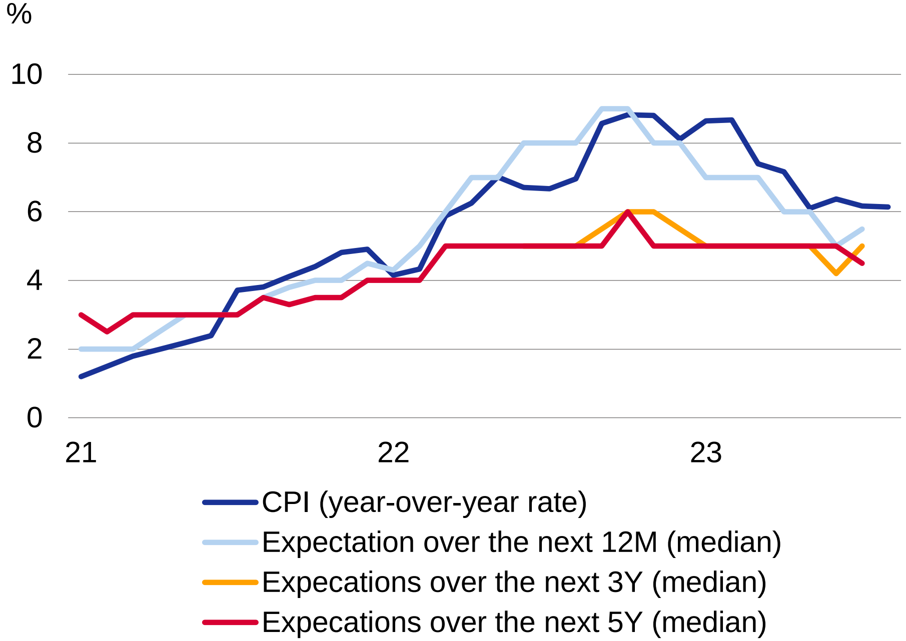
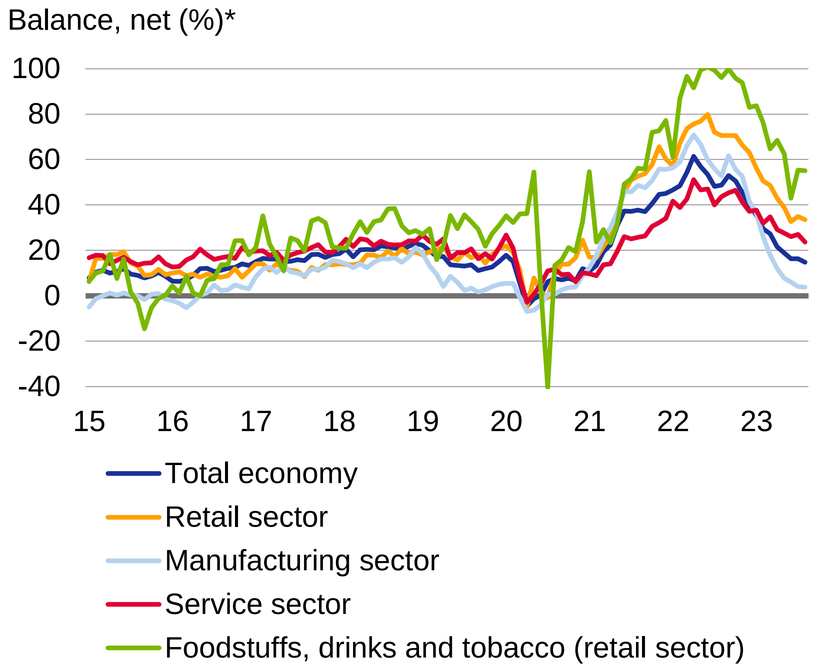
Medium-term inflation expectations are still elevated, selling price expectations eased from extreme levels

Inflation expectations by private households vs. actual inflation



Sources: WEFA, Haver Analytics, Federal Statistical Office, Deutsche Bundesbank

Selling price expectations (ifo survey)



* Balance of opinion (seasonally adjusted) regarding the expected selling prices over the next three months. Positive (negative) values signal upward (downward) price pressures.

Sources: WEFA, ifo, Deutsche Bank Research

- Private households expect the inflation rate to reach a still high level of 4.5% (median) in five years time.
- Firms' selling price expectations for the next three months eased substantially, though from very high levels.

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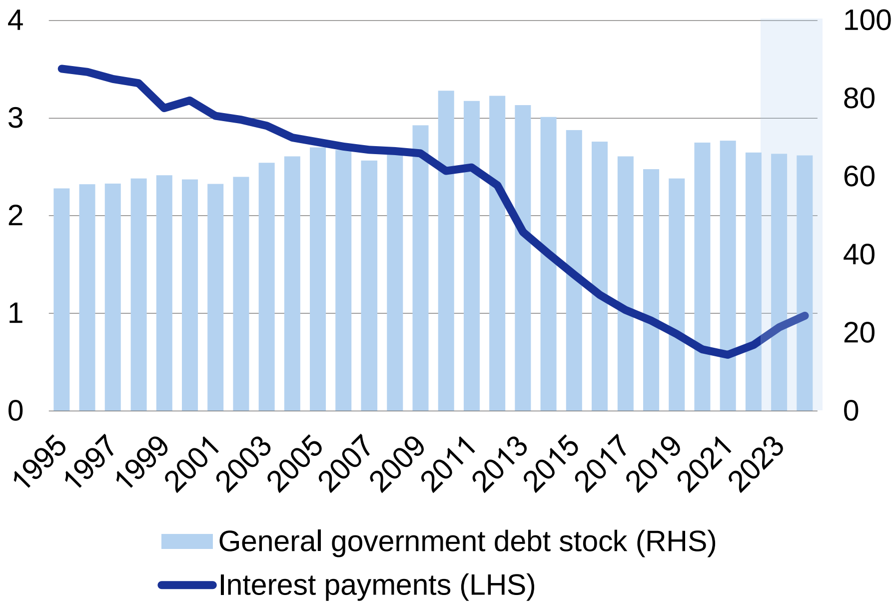
Budget impact from energy price shock might be less severe, but debt interest payments are set to increase strongly

Interest payments are projected to rise strongly from low levels

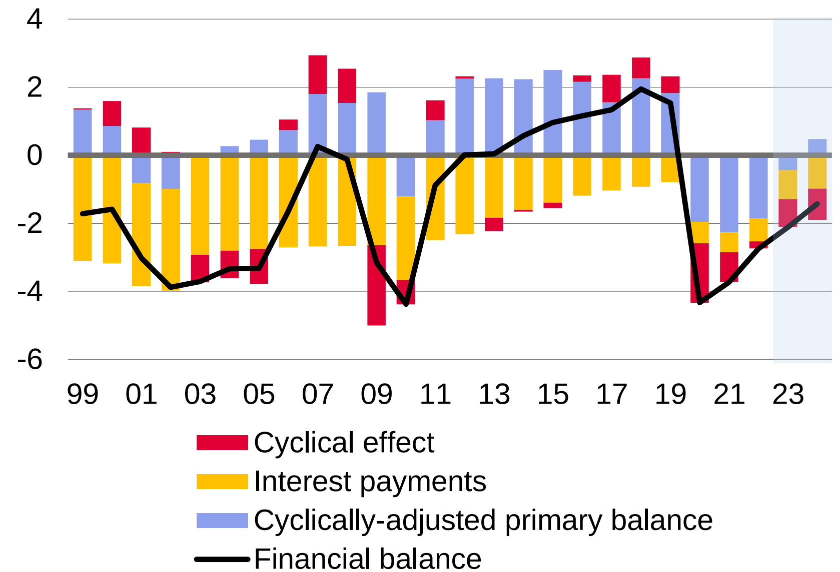
% of GDP (gen. gov. level) (national accounts)



Sources: WEFA, Federal Statistical Office, Eurostat, Deutsche Bank Research

General government budget outlook in the baseline scenario

% of GDP (gen. gov. level) (national accounts)



Sources: WEFA, Federal Statistical Office, AMECO, OECD, Federal Ministry of Finance, Deutsche Bank Research

- The general government deficit (Maastricht definition) narrowed to “just“ 2.7% of GDP in 2022 (from 3.7% of GDP in 2021) as pandemic-related spending tapered off.
- Given the plunge in wholesale electricity/gas prices – which is set to reduce the government‘s cost for the energy price subsidies – we expect the fiscal deficit to narrow further to 2.1% in 2023 and 1.4% in 2024.

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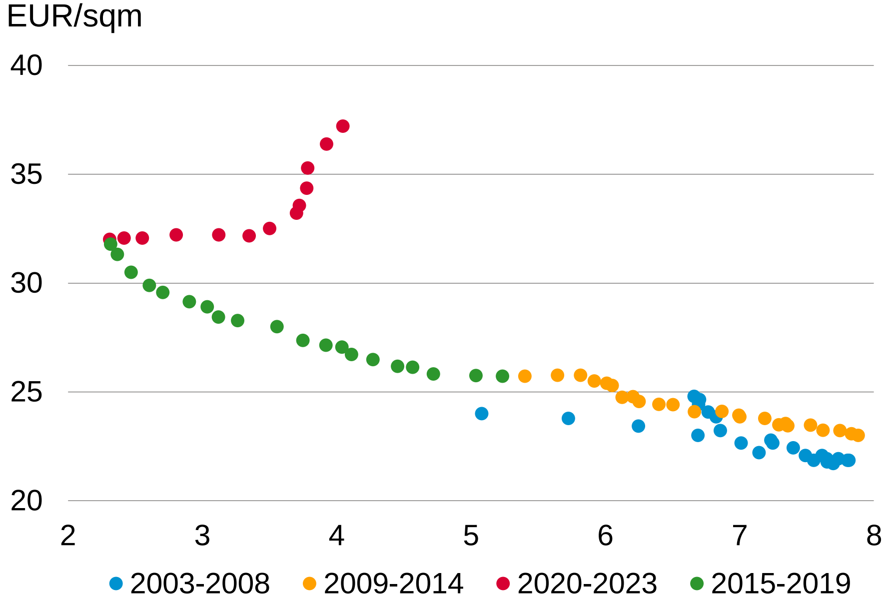
Infrastructure bottlenecks could be an understated obstacle to office demand, especially in A cities

2003-2022 Office market in A cities: Average top rent vs. vacancy rate



Sources: bulwiengesa, Deutsche Bank Research

Office space vacancy rate in %

City class	A	B	C	D
# Obs	7	14	22	83
1990-2022 average	6.1	5.3	4.9	5.4
2019	3.2	3.1	4.1	4.6
2020	3.8	3.5	4.2	4.4
2021	4.8	3.8	4.1	4.0
2022	5.0	3.9	4.1	3.9

Source: bulw iengesa, Deutsche Bank Research

- Given the developments in the US, the German office market has also come under scrutiny. While relevant survey indicators have deteriorated in recent times, the market developments are limited compared to the US.
- Vacancy rates (4.5%) in the office market have only slightly increased and we expect them to stay below the long-term average of 5.4%.
- Infrastructure bottlenecks in metropolises might be an important and hitherto neglected argument in the debate. Among other things, this could actually lead to a higher WFH share regionally and thus keep vacancy rates in A cities elevated, relative to smaller towns.

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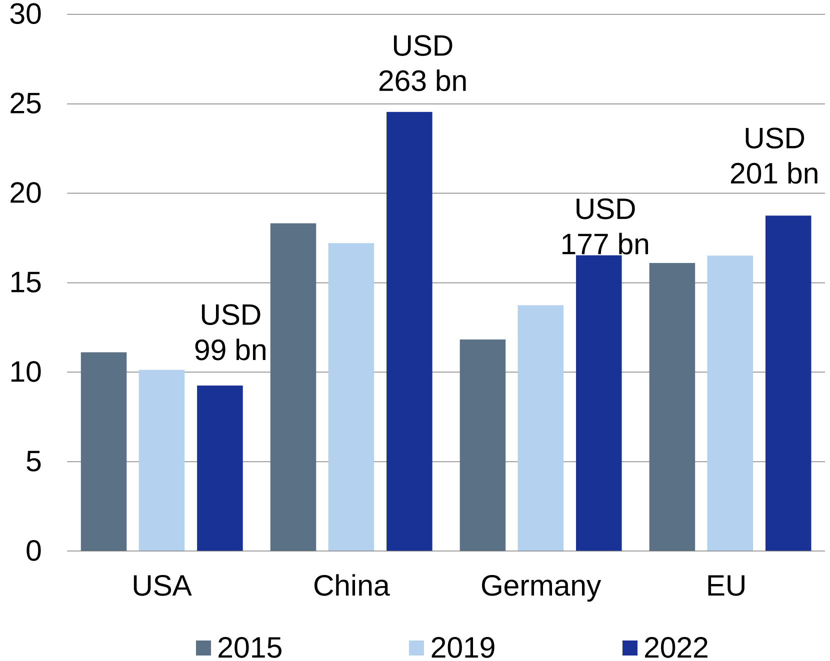
Green trade surpluses – comparing Germany with China

China, Germany (and thus the EU) are gaining market share

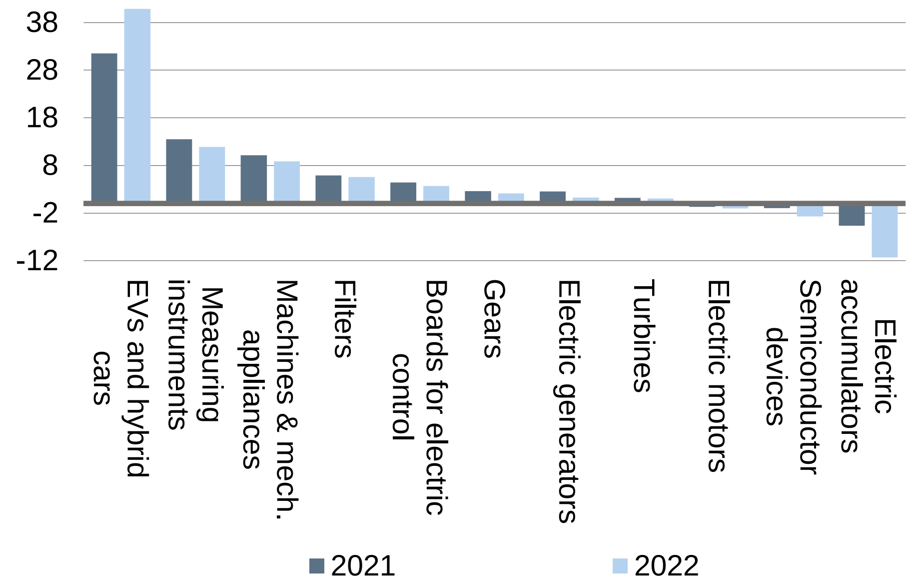
% of total global LCT exports



Source: UN Comtrade, Deutsche Bank

EVs, measuring instruments and machinery top the list

Net German LTC exports by product, USD bn



Source: UN Comtrade

- The global export market for low-carbon-technology products is growing faster than total manufactured goods exports. EVs, hybrid cars, measuring instruments and machines drive Germany's green trade surplus.
- China registered the largest green trade surpluses in 2022 and looks set to remain the green net export world leader over the next few years. While we expect Germany to maintain its green trade surplus over the next couple of years, fight for market share is intensifying.(see our recent note)

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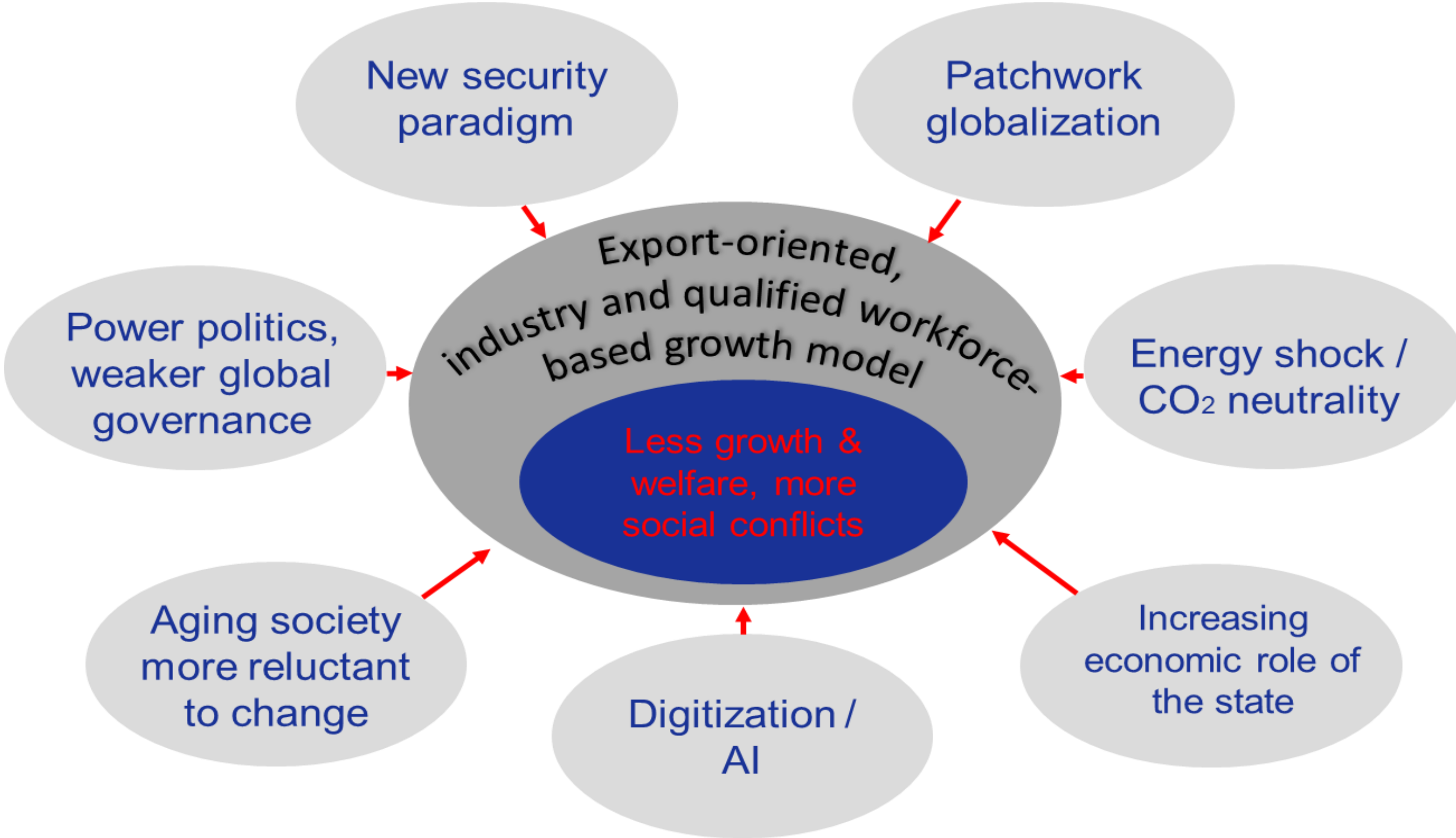
Germany's current challenges are substantially more complex than in the previous "sick man of the EUR" episode



- In a historic review (Focus Germany "Midterm Review", pp. 3-10) we revisit the challenges Germany was facing when it was once called the "sick man of the euro" and which policy measures turned the country around.
- There are interesting parallels to today's situation. This time the Ukraine war has knocked off three pillars of Germany's economic success, which together with other adverse structural changes make a turnaround much more challenging.

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Appendix 1
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