Germany’s Economic Outlook

Chewing gum cycle, bubble gum risks

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Forecasting Center
Chewing gum-type business cycle

- Stretched upswing, faint cyclical pattern
- Migration feeds markedly into potential growth (delayed for refugees)
  » 2015: + 331,000
  » 2016: + 511,000
  » 2017: + 313,000
  » 2018: + 213,000
- Capacities already slightly over-utilized
Capacity utilization above normal and increasing

- **Manufacturing**
  - Upward trend, third year of over-utilization ...
  - ... incoming orders exceed production capacities

- **Construction**
  - Record-high capacity utilization

- **Services**
  - Lack of demand (ifo) on record-low levels

- **Vibrant labor market**
Data edge: High momentum

- *ifo climate brightened up*
  - Situation: 4-years high
  - Expectations: Pronounced improvement since August

- Incoming orders on the rise

- Industrial production: upward trend since 2012

- **2017: Dampening working-day effect (0.3 ppt)**

**Gross domestic product**

![Graph showing GDP growth with qoq-change (rhs) and level lines, with years and corresponding percentage values.](image-url)
Booming construction sector

- **Record-high capacity utilization**
- **Swelling order books**
  - Total: + 21 % (Q3, y-o-y)
  - Dwellings: Second year of two-digit rates
- **Price pressure**
  - Value added: > 5 percent (two years in a row)
  - Real estate transactions (vdp)
    - 2014: + 3.1 %
    - 2015: + 4.5 %
    - 2016: + 5.8 % (Q1 to Q3)
Stimulating environment for construction spending

- Driving force: housing
  - Mortgage interest rates at record-low levels
  - Dynamic labor market

- High government revenues

- Growth contributions
  - 2016: 0.3 ppt
  - 2017: 0.3 ppt
  - 2018: 0.4 ppt

Constructions

<table>
<thead>
<tr>
<th>Quarter</th>
<th>qoq-change (rhs)</th>
<th>Level</th>
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<tbody>
<tr>
<td>I 2014</td>
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<td>II 2015</td>
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<td>IV 2018</td>
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Quarterly data: seasonally and working-day adjusted.
GFCF: Stretched upswing, small accelerator effects

- Flat cyclical pattern
- Gross fixed capital formation gradually gaining momentum

**Investment cycles**

- Output gap (rhs)
- GFCF
- Machinery and equipment

Annual data.
GFCF, machinery and equipment: volumes, change on previous year;
Output gap: in percent of potential output.
Dampened dynamics in M&E spending

- 2017 (yoy)
  - Carry-over effect (- 0.5 ppt)
  - Working-day effect (- 0.8 ppt)

- 2018
  - Topping pre-crisis level

- Weak dynamics compared to historical standards
- Financing conditions
  - Record-low credit costs
  - Hardly any credit hurdles
- Low market uncertainty, but increased policy uncertainty
- Harbinger of demographics?
Exports back on track

- Recovered incoming orders
- German export markets
  - Lower uncertainty
  - Improved business climate
- Export market growth
  - 2016: + 2.1 percent
  - 2017: + 2.2 percent
  - 2018: + 2.4 percent
- Risks
  - Brexit
  - Neo-protectionism (US: micro-interventionism?)
Brexit: Impact on German growth

- Country-specific export function
  - UK-GDP
  - Exchange rate GBP/EUR
- UK-GDP [autumn forecast]
  - 2016: + 2.0 % [+ 1.6 %]
  - 2017: + 1.2 % [+ 0.6 %]
  - 2018: + 1.6 % [+ 1.6 %]
- More pronounced devaluation of the British pound: 8 + 3.5 percent
- Impact on exports in the UK (cumulated)
  - 2016: – 2.2 %
  - 2017: – 8.2 %
  - 2018: – 10.0 %
- Impact on GDP (cumulated): < 0.5 %
Higher oil prices weigh on purchasing power

Private consumption

- qoq-change (rhs)
- level

2010 = 100

Percent

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<thead>
<tr>
<th>2014</th>
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Savings rate

Disposable income

Deflator

Private consumption (rhs)

Contributions to change in private consumption

Savings rate

Disposable income including change in pension entitlements.

Annual data.
Internal and external driving forces

- 2015/2016: strongest increase in consumption in 15 years
- Gradually growing investment pillar
- Exports recovering

Expenditure-side components to GDP-growth

- Consumption
- GFCF
- External trade
- Inventories

Annual data; price-adjusted, Lundberg components.
## Labor market regains momentum

### Supportive effective wages (hourly)
- 2016: + 2.6 %
- 2017: + 3.1 %
- 2018: + 3.0 %

### Registered unemployment [vs. ILO rate]
- 2016: 6.1 % [4.0 %]
- 2017: 5.9 % [3.7 %]
- 2018: 5.6 % [3.1 %]

### Employment

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<tr>
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<td>334</td>
<td>394</td>
<td>438</td>
<td>386</td>
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<td>2018</td>
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Quarterly data: seasonally adjusted.
Annual data: yoy differences in 1,000 persons.
Refugees gradually showing up on the labor market

Unterbeschäftigte, arbeitslose und beschäftigte Flüchtlinge 2015-2016

Einfluss der Flüchtlinge auf Arbeitslosigkeit und Unterbeschäftigung 2012-2016
### Key figures

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<th>2015</th>
<th>2016</th>
<th>2017</th>
<th>2018</th>
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</thead>
<tbody>
<tr>
<td>GDP (%)</td>
<td>+ 1.7</td>
<td>+ 1.9</td>
<td>+ 1.7</td>
<td>+ 2.0</td>
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<tr>
<td>GDP deflator (%)</td>
<td>+ 2.0</td>
<td>+ 1.4</td>
<td>+ 1.3</td>
<td>+ 1.9</td>
</tr>
<tr>
<td>Consumer prices (%)</td>
<td>+ 0.2</td>
<td>+ 0.5</td>
<td>+ 1.5</td>
<td>+ 1.8</td>
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<td>Unit labor cost, hourly (%)</td>
<td>+ 1.5</td>
<td>+ 1.2</td>
<td>+ 1.6</td>
<td>+ 1.8</td>
</tr>
<tr>
<td>Employment (1000 persons)</td>
<td>43,058</td>
<td>43,495</td>
<td>43,881</td>
<td>44,390</td>
</tr>
<tr>
<td>Unemployment (1000 persons)</td>
<td>2,793</td>
<td>2,691</td>
<td>2,643</td>
<td>2,547</td>
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<tr>
<td>Public net lending (% of GDP)</td>
<td>0.7</td>
<td>0.5</td>
<td>0.4</td>
<td>0.5</td>
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<tr>
<td>Current account balance (% of GDP)</td>
<td>8.4</td>
<td>8.7</td>
<td>8.2</td>
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Stability risks

- Ultra-expansionary monetary policy: Time matters!
  - Distortion of price and production structures
    - Capital stock
    - Exchange rate
  - Financial stability
    - Depressed risk premia (too few insolvencies, delayed structural change)
    - Overstretched maturity transformation

- Over-estimating potential output growth
  - Data edge problem (procyclical distortion)
  - Demographics: interim relief (integration of refugees?)

- Hardly any vigor in terms of growth policies
- Call for stimulus programs within the EMU context
- Neo-protectionist tendencies in the world economy