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The R-question

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Germany's economy. The R-question. Given much weaker than expected January business surveys and in particular the slump in their more forward-looking components we are now expecting the German economy to contract again in Q1 2019. Due to the yet unknown Q4 GDP outcome and its contradictory signals we currently refrain from formally revising our 1% GDP forecast lower again, but are expecting to shave off several tenths of a percentage point come February 22nd, unless the Statistical Offices Q4 GDP breakdown – and the new monthly data available by then – provide us with substantial positive surprises. While a technical recession might be avoided by a hair's breadth with a positive Q4 number, the development of several key cyclical indicators is telling us that the German economy is drifting towards recession right now.

Cyclical spark does not ignite investment growth. In 2018, investment in machinery and equipment grew by 4.5% in real terms in Germany. However, we expect this rate to slow to significantly less than 3% p.a. in 2019 and 2020 already, whereas downside risks currently predominate.

Record surplus despite economic downturn – does Germany need fiscal stimulus now? Despite the slowdown the general government posted a record surplus of ca. EUR 59.2 bn (1.7% of GDP) in 2018. Still, the years of fiscal plenty seem to be coming to an end as the growth outlook deteriorates. We forecast the surplus to shrink to 1% of GDP in 2019 and 0.8% of GDP in 2020. In light of the economic downturn policymakers have called for tax cuts to prop up growth. In our view, tax cuts may be a structural but not a cyclical necessity given that the output gap is still positive.

The view from Berlin: Looking beyond Brexit: German politics will heat up in the course of 2019. The German government backs the EU's stance on the Brexit negotiations. In contrast, the Groko is divided on economic and tax policy. While corporate Germany hopes for substantial tax relief including better conditions for R&D investment to enhance competitiveness, recent debates have focused on (re-)distribution – the evergreen – and an alleged necessity of strengthening domestic demand. The conflict is likely to intensify, given FM Scholz' rejection of the CDU/CSU's demand for lower corporate taxes and a quick and complete abolishment of the income tax solidarity surcharge. In autumn CDU and/or SPD defeats in the three eastern German state elections could even trigger snap elections.

Economic forecasts

	Real GDP (% growth)			Consumer Prices* (% growth)			Current Account (% of GDP)			Fiscal Balance (% of GDP)		
	2018	2019F	2020F	2018	2019F	2020F	2018	2019F	2020F	2018	2019F	2020F
Euroland	1.8	1.2	1.3	1.7	1.4	1.7	2.7	2.3	2.0	-0.8	-1.0	-1.0
Germany	1.5	1.0	1.4	1.9	1.7	1.4	7.1	6.4	6.0	1.7	1.0	0.8
France	1.5	1.4	1.3	2.1	1.0	1.9	-0.4	-0.3	-0.2	-2.5	-3.2	-2.0
Italy	0.8	0.7	0.9	1.2	1.3	1.6	2.5	2.2	2.2	-2.2	-2.8	-2.7
Spain	2.5	2.4	2.1	1.7	1.5	2.1	1.4	1.2	1.0	-2.7	-2.2	-1.8
Netherlands	2.5	1.9	1.8	1.6	2.2	1.8	10.2	9.9	9.7	0.8	0.6	0.4
Belgium	1.5	1.4	1.4	2.3	2.1	1.8	0.3	0.4	0.5	-1.1	-1.3	-1.4
Austria	2.6	1.9	1.8	2.1	1.8	1.8	2.2	2.3	2.5	-0.2	0.1	0.3
Finland	2.4	1.9	1.8	1.2	1.2	1.6	-0.5	0.0	0.5	-0.7	-0.7	-0.6
Greece	2.0	1.9	1.8	0.8	1.5	2.5	-1.0	-0.6	-0.3	0.6	1.1	1.3
Portugal	2.2	1.7	1.5	1.2	1.1	1.8	-0.1	0.0	0.0	-0.8	-0.7	-0.6
Ireland	6.4	3.4	3.3	0.7	0.9	1.2	11.0	10.0	9.0	0.0	0.0	0.3
UK	1.3	1.6	1.4	2.5	2.0	2.1	-3.5	-3.3	-3.0	-1.1	-1.4	-1.4
Denmark	1.5	1.9	1.7	0.7	1.5	1.8	6.1	6.2	6.1	0.1	-0.2	0.2
Norway	2.4	2.1	2.0	2.8	2.1	2.0	6.2	6.0	6.1	5.4	5.3	5.2
Sweden	2.4	2.0	1.9	2.0	1.9	1.9	2.8	3.1	3.1	1.1	0.9	0.6
Switzerland	2.6	1.4	1.6	0.9	0.8	1.1	10.3	10.3	10.7	0.7	0.5	0.4
Czech Republic	3.0	2.9	2.8	2.1	2.0	1.9	0.7	0.6	0.5	1.0	0.4	0.1
Hungary	4.7	3.6	3.1	2.9	2.9	3.0	1.9	1.5	1.2	-2.3	-2.0	-1.8
Poland	5.1	3.5	3.2	1.8	2.4	2.9	-0.6	-0.7	-0.9	-1.0	-1.8	-2.4
United States	2.9	2.5	2.1	2.4	1.5	2.2	-2.5	-3.5	-3.5	-3.9	-4.6	-4.5
Japan	0.7	0.7	0.2	1.0	0.4	0.7	3.5	3.6	4.1	-2.5	-2.2	-2.0
China	6.6	6.1	6.0	2.1	2.4	2.6	0.4	-0.2	-0.4	-3.5	-4.5	-4.0
World	3.8	3.5	3.5	3.3	3.1	3.1						

*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

					2019				2020			
	2017	2018F	2019F	2020F	Q1	Q2	Q3F	Q4F	Q1F	Q2F	Q3F	Q4F
Real GDP	2.2	1.5	1.0	1.4	-0.2	0.3	0.4	0.3	0.2	0.2	0.3	0.2
Private consumption	1.8	1.0	1.1	1.4								
Gov't expenditure	1.6	1.1	1.7	1.3								
Fixed investment	2.9	3.1	3.2	2.8								
Investment in M&E	3.7	4.5	2.7	2.4								
Construction	2.9	3.0	4.2	3.8								
Inventories, pp	0.1	0.4	0.3	-0.1								
Exports	4.6	2.4	2.1	3.2								
Imports	4.8	3.4	3.7	3.9								
Net exports, pp	0.2	-0.2	-0.6	-0.1								
Consumer prices*	1.7	1.9	1.7	1.4								
Unemployment rate, %	5.7	5.2	4.9	4.8								
Industrial production**	2.9	1.5	0.5	1.0								
Budget balance, % GDP	1.0	1.7	1.0	0.8								
Public debt, % GDP	63.9	60.0	57.2	54.5								
Balance on current account, % GDP	8.0	7.1	6.4	6.0								
Balance on current account, EUR bn	261.2	241	226	220								

*Inflation data for Germany based on national definition. This can lead to discrepancies to other DB publications. **Manufacturing (NACE C)
The actual figures for Germany's GDP in Q4 including subcomponents have not yet been published. Therefore, we only provide our quarterly growth forecasts for real GDP.
Sources: Federal Statistical Office, German Bundesbank, Federal Employment Agency, Deutsche Bank Research

Germany's economy: The R-question

The start of the German economy into 2019 has been a major disappointment so far. While a few weeks ago the Statistical Office sounded rather optimistic that the economy might have eked out a modest increase in Q4 2018 – overcoming the 0.2% drop in Q3 –, the recent across the board disappointing dataflow has increased concerns that this might have been a too optimistic judgement.

Either way, even if the Stats Office confirms its assessment on February 14th (when it publishes its flash estimate for Q4), we are now expecting the German economy to contract again in Q1 2019. The much weaker than expected January business surveys and in particular the slump in their more forward looking components are clearly pointing into this direction. The ifo survey's expectations component nose-dived by 3.1 points. The third-largest decline since 2007. The PMI survey was weighed down by strong declines in the assessment of new order inflow in industry but now also in services.

Global economic policy uncertainty jumped in December marking a new all-time high. Most of the global trouble spots (Brexit, Chinese growth concerns) have taken a turn for the worse in January, making it very hard to assume a fundamental improvement during the reminder of Q1. One glimmer of hope might be provided by the US-Chinese trade negotiations. But we have learned to discount any "breakthroughs" as previous "deals" too often failed to deliver. Even more worrisome, a perceived success over China might encourage the US administration to turn to Europe where the trade conflict is currently on hold while consultations are under way. This is certainly a major concern for the battered German car industry, where the hope for recovery following the WLTP-induced slump has been painfully slow while new problems are already creeping up (strikes among suppliers, misrepresentations regarding mileage).

Granted model-based recession probabilities are not yet flashing red, but such models usually send clear signals only three to six months after the start of a recession as an analysis of the German council of economic experts has impressively shown for the 2008/09 recession. In their more qualitative assessments economists – notwithstanding the few brave ones who "called the recession" – tend to pooh-pooh recessionary developments sugar-coating them as "the result of temporary factors" or "the upswing taking a breather" until the recession hits them in their face (status quo bias). In defence of us poor economists one can point to the non-linearities kicking in when an economy transits into recession. There is a tipping point when the entrepreneurs' and consumers' processing mode for new information changes and the confirmation bias which prevented them from admitting the onset of a recession so far is causing them to all of a sudden see recession signals everywhere they look. In such a regime monetary policy is extremely challenged even when interest rates are at more normal levels. These tipping points can unfortunately not be identified in real time, but we are seriously worried that we might have hit one.

Due the yet unknown Q4 GDP outcome and its contradictory signals we currently refrain from formally revising our 1% GDP-forecast lower again, but are expecting to shave off several tenths of a percentage point come February 22nd, unless the Statistical Offices Q4 GDP breakdown – and the new monthly data available by then – provide us with substantial positive surprises. While a technical recession might be avoided by a hair's breadth with a positive Q4 number, the development of several key cyclical indicators is telling us that the German economy is drifting towards recession right now.

Did the economy really expand in Q4?

Following the decline in GDP by 0.2% in Q3, the German Federal Statistical Office had two weeks ago suggested a slight improvement again for the final quarter. In light of the poor performance in industrial production in November (-1.9% compared with the previous month) and the ongoing declines observed by ifo and the PMI, this confidence came as a surprise at the time. After the 4.3% slump in retail sales in December published on 31 January, another fall in GDP seems – at least based on our bridge models – quite possible and in particular, if industrial production has not increased by much more than 2% in December, which seems unlikely in light of the poor survey results (consensus estimate +0.8%). However, the German Federal Statistical Office pointed out that it usually receives a very high number of late notifications regarding December retail sales, which has resulted in an upward revision of 2.5 percentage points on average over the last five years. Yet even if that is also the case this time, GDP could still have dropped.

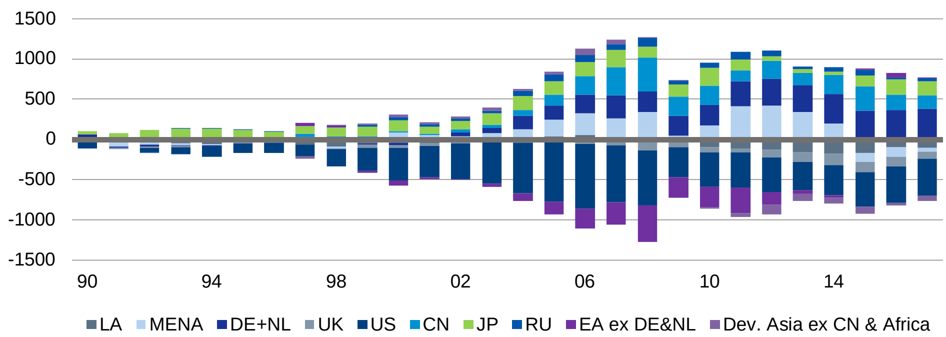
Economists are blind when it comes to recession

Economists find it very difficult to predict economic turning points. Their track record when it comes to identifying recessions at an early stage is even worse. On the outbreak of the major financial and economic crisis in 2007, the Chief Economist of the OECD declared that "for the OECD area as a whole, growth is set to exceed its potential rate for the remainder of 2007 and 2008, supported by buoyancy in emerging market economies and favourable financial conditions".[1] The German Council of Economic Experts published similar observations in its annual report in November 2007, confirming the "systemic financial market crisis", but predicting growth of 1.9% for 2008 and declaring that this drop in momentum "should not be seen as an indication that the upturn has run its course or even that a recession is around the corner".

The warning signs of the 2008/2009 recession were actually glaringly obvious, at least in hindsight: Massive current account imbalances in large economies and the dramatic build-up of household and public borrowing, which was promoted by monetary policy that was too expansionary. Whether this gain in insight will prove beneficial in helping us identify the next recession remains unclear, at least for now.

Global imbalances 1

Current accounts, bn USD



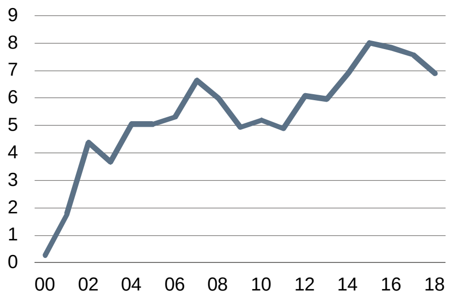
Sources: IMF, Deutsche Bank Research

These days it is often argued that the situation on both of these fronts has calmed down and therefore that concerns about an imminent recession in the

[1] Cotis, J.P. (2007). 'Overview', OECD Economic Outlook, May, OECD.

Germany: Net exports 2

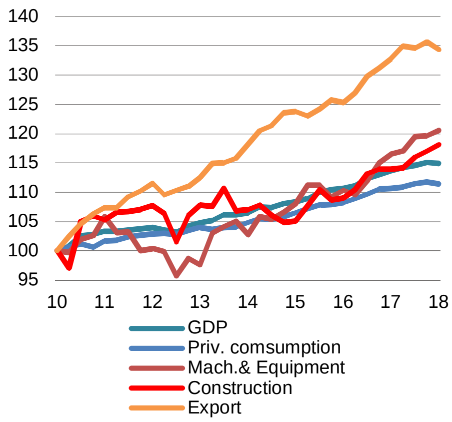
% of GDP



Source: Deutsche Bank Research

Exports: Strong driver of the 9-year GDP expansion 3

Q3/2010 = 100



Sources: Deutsche Bank Research, Deutsche Bundesbank

eurozone or Germany at least are exaggerated. In fact, global current account imbalances have significantly decreased since 2008, even though the level they are at is still high when viewed over the longer term.

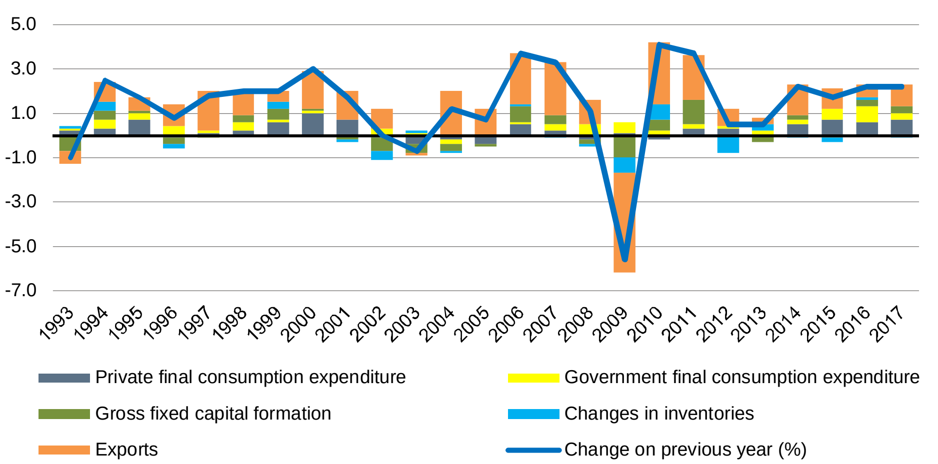
Unfortunately Germany's dependency on exports has fallen only slightly to 6.9% in 2018 since its peak of 8% in 2015, as measured by the share of net exports to GDP. Yet this level is still slightly higher than it was in 2007/2008.

Germany is still very much dependent on exports

Chart 3 clearly shows how much exports drove the recovery of the German economy**.** Net exports fell by 0.2pp in 2018, this number, however, significantly understates the real significance of exports. In its latest annual report, the German Council of Economic Experts distributed the proportionate imports to the expenditure components on the basis of the input/output analysis, rather than merely deducting them from exports. As a result, contributions to growth from private consumption and investment fell significantly while (actual) net exports still accounted for almost half of GDP growth in 2017, at just under one percentage point. As calculated, net exports probably increased slightly in 2018 and did not cost 0.2 percentage points of growth as reported in the national accounts (Chart 4). This view also qualifies the common opinion that the upturn was recently driven only by domestic demand, making the German economy relatively immune to foreign economic disruptions.

Growth contributions correct for import content* 4

pp



*With this method, the import share of each expenditure component is estimated and import-adjusted values are calculated on this basis. The import-adjusted growth contribution of a component measures its contribution to real GDP growth.

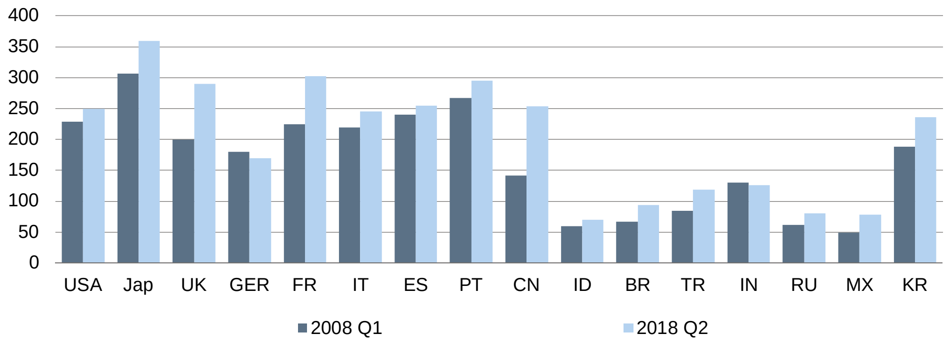
Source: German Council of Economic Experts

The borrowing situation gives us even less reason to declare the all-clear, at least internationally. While some European countries heavily affected by the sovereign debt crisis significantly reduced business and household borrowing, it has risen significantly in some emerging markets, in China in particular. Add to that the fear that the extremely long period of near-zero interest rates probably has created some zombie companies even in Germany, which should have left its imprint in the quality of banks' loan books. Apart from a few exceptions, progress concerning public debt has also been modest.

What actually is a recession?

Total debt has increased since 2008 | 5

Debt (excluding financial sector) in % of GDP



Source: BIS

The question about the probability of a recession requires us to define how the term recession is to be understood. For the general public, it is often understood to be a decline in real GDP from the previous quarter in two consecutive quarters (technical recession). This simple rule makes it relatively easy to identify. However, this type of decline can also be caused by a unique development in a key sector of the economy or also by temporary events. This is why, in economic practice (as for example by the National Bureau of Economic Research – NBER), a recession is defined as a significant decline in activity spread across the economy, visible across a range of macroeconomic indicators, lasting more than a few months.[2] In its 2008 annual report, the German Council of Economic Experts defined a recession "as a decline in relative output gaps by at least two-thirds of the respective potential growth rates (i.e. in Germany that would currently mean just under 0.9pp given a potential growth rate of around 1¼%, which is accompanied by an effective negative output gap".[3] According to this definition, a clear downward trend can start to be called a recession if the economy as a whole is in a phase of under-utilisation. Since the German economy still enjoyed a very positive output gap of approximately 1.5pp at the end of 2018, the risk of a recession in 2018 – at least according to this definition – would be extremely low. The problem with this approach, however, is the difficulty in forecasting the output gaps in real time. Most (filter) procedures used for this indicate substantial uncertainties in an unfinished cycle and therefore sometimes undergo major revisions in subsequent years. For the timing of recession phases, the German Council of Economic Experts therefore adopts a similar approach to NBER.

As we have seen how difficult it is to define a recession, the often cited expression, "It may not be a recession, but it sure feels like one", is not surprising.

[2] https://www.nber.org/papers/w14221.pdf
[3] https://www.sachverstaendigenrat-wirtschaft.de/fileadmin/dateiablage/download/gutachten/ga08_ges.pdf

Is Germany perhaps already in a recession?

Technically speaking, arguably not yet. At least, the German Federal Statistical Office talked about "a slight rise in the fourth quarter" when referring to initial calculations of German GDP in 2018[4] at its press conference on 15 January. However, the Office did warn of the tentative nature of this statement due to the lack of data available at the time. The Office did have access to the low November figures for industry (production –1.9%, nominal sales –2.4%, compared with the previous month in each case), but where production in December is concerned, the statisticians were none the wiser. (The December production and export figures will be published on 7 and 8 February. The retail figures for December published recently were disappointing, even if we assume that they are likely to undergo a significant upward revision. The report on the GDP in the fourth quarter will be released on 14 February. While the assessment of production development in comparison with the previous month temporarily improved in December's Purchasing Managers' Index (PMI) (51.5 from 50.3), the decrease in the production assessment in the ifo index compared with the previous month continued unabated (100.5 from 102.3) – in January, it then slumped to 94.6, the lowest point since December 2012. Our GDP bridge equation produced a GDP rise of barely 0.1% in Q4 based on the values for industrial production and retail sales (up to November in each case). Considering the margin of error of +/- ¼%, GDP might well have dropped in Q4. However, it would be extremely unusual if the German Federal Statistical Office's press release on GDP in Q4 was to completely revise its positive assessment from mid-January.

ifo index: Levels 1m prior to the recession start* 6

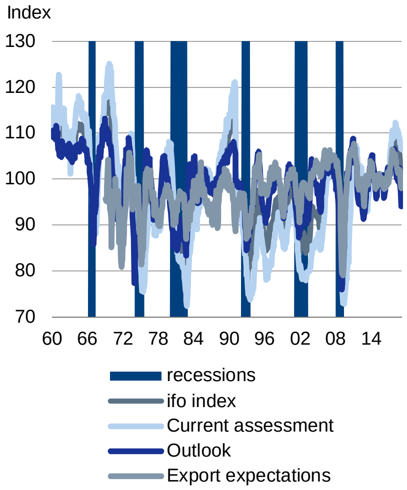
Old index: 2005 = 100

	Index	Current assessment	Business expectations	Export expectations
Average	97.0	98.9	95.3	98.6
Min:	86.6	92.9	79.4	95.2
Max:	106.4	109.1	103.8	104.4
Jan-19	100.0	106.4	94.0	98.0

*as defined by the SVR

Source: ifo

ifo levels in line with previous recession starts 7



Source: ifo

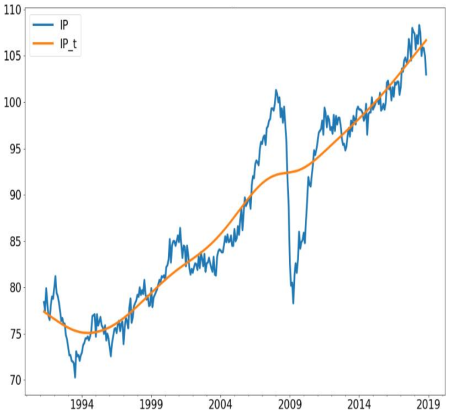
ifo business climate level does not contradict a recession

The still relatively high level of survey indicators such as the PMI for the economy as a whole (52.1) or the ifo index of 99.1 (or 100.0 in its former definition) can only assuage concerns about an impending recession to a limited extent. In Table 6, based on the six recession phases defined by the German Council of Economic Experts since 1960, we provide an analysis of the relevant ifo index values one month before the official start of the recession (the dates are available from the Council on a monthly basis). Please note that the German Council of Economic Experts sets the start of a recession using the upper turning point in the cycle. The levels from January 2019 are relatively close to the average from past recessions, only the assessment of the current situation is significantly higher at the moment.

[4] https://www.destatis.de/DE/PresseService/Presse/Pressekonferenzen/2019/BIP2018/Bruttoinlandsprodukt_2018_Uebersicht.html

Industrial production: Below trend and falling 8

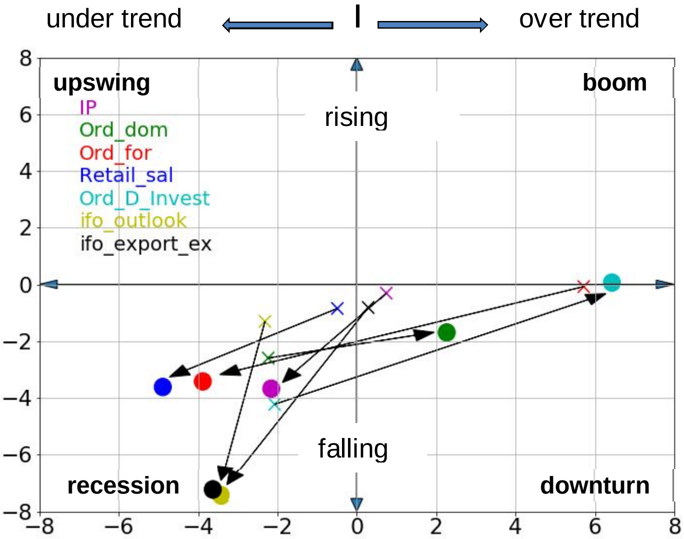
2015=100



Sources: Deutsche Bundesbank, Deutsche Bank Research

An analysis of key economic indicators such as production, orders received, their subgroups or the components of the ifo index in view of their variation and their situation in relation to their long-term trend, e.g. like they are employed in so-called business cycle clocks, shows that many indicators have ended up in the recession quadrants (declining or below trend) in the last few months. Only domestic orders for capital assets appear to be back in “normal” territory again after their 6.6% rise in November (October –6.0%). Large orders played a key role in both the decline in October and the strong countermovement in November.

Key economic indicators are in the recession zone 9

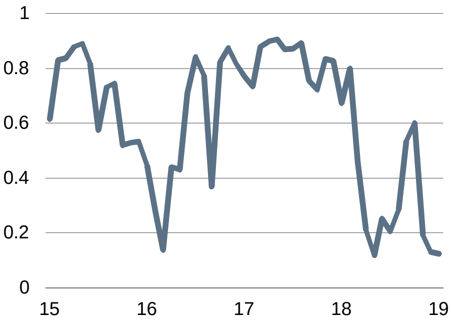


● = last value / x = 3 months ago

Quellen: Deutsche Bundesbank, ifo, Deutsche Bank Research

Probability of an economic expansion* 10

1 represents the highest probability of economic expansion



*recession probabilities based on Markov regime switching model. Estimated values based on first differences of monthly ifo business climate index.

Sources: ifo, Deutsche Bank Research

Models for the probability of a recession (still) lack reliable signals

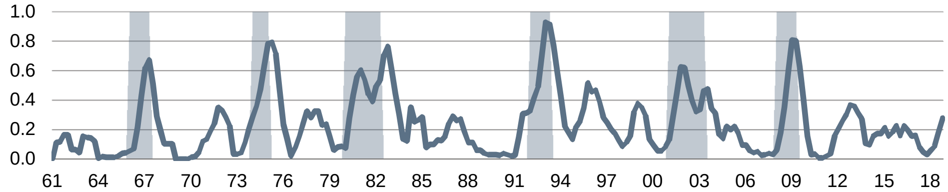
Markov switching models or probit models are usually used to deduce the probabilities of a recession from the development of individual or a group of economic indicators. Markov models are based on the identification of different statistical properties of a time series (mean, variance) in upturn and downturn/ recession phases and determine transition probabilities between the two regimes. Our model is based on the ifo business climate and shows that the probability of the German economy being in an expansion phase fell to around 10% in January. However, the use of a sentiment indicator, which is more likely to involve stronger fluctuations than hard economic indicators (such as production or sales), results in comparatively volatile signals, thereby reducing the reliability of the signal.

Probit models involve a type of regression where the different economic indicators and/or financial market indicators can assume only two values, e.g. 1 for “recession” and 0 for “no recession”. Our probit model charts a clear jump in the probability of recession in the final quarter to 28%. Yet the graph (Chart 10) shows that similarly high values were sometimes temporary in the past and resulted in a total of seven false indicators. On the other hand, all recessions – with the exception of the 1992/1993 recession – started with much lower values.

In conclusion, this analysis shows the probability of us currently being in a recession is just under 50%.

Probit model*: Rising recession risks but no certainty (yet) 11

Probability of recession: 1.0 = 100 %; 0.0 = 0 %

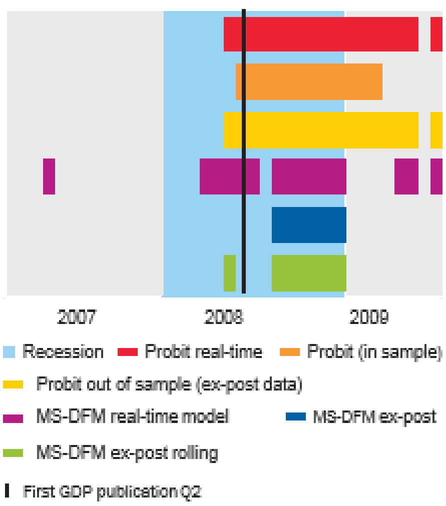


*to estimate recession probabilities we utilise a probit model. Dependent variable is a binary recession indicator of the German Council of Economic Experts. As controls we include new orders, ifo
business climate index, industrial production (excluding construction) as well as corporate bond yields. Presented values are four
Sources: ifo, Destatis, Deutsche Bank Research

An analysis carried out by the German Council of Economic Experts that looked into the question of if and when these types of approach would have indicated the 2008/2009 recession[5] also concluded with a disappointingly indifferent result. The probabilities defined by the Markov and probit models were only clearly revealed three to six months after the start of the recession that had been ongoing since February 2008.

Transmission mechanisms change over time

Identification of 2008 recession* 12



* For each model, months with an estimated recession probability of over 50% are defined as recession months.

Source: German Council of Economic Experts

Moreover, the experience of the global financial and economic crisis, which began in 2007 and led to the most recent recession in Germany in 2008/2009, suggests that the transmission mechanisms, which spread negative economic momentum throughout the economy and ultimately push it into a recession, could have significantly changed in the last few decades. These assessments, which diminish confidence in these types of model, are likely to be even more relevant as a result of the in many respects exceptional upturn phase since 2009 (duration, unexpectedly subdued price development and not least the unorthodox monetary policy of major central banks).

Predicting a recession: Notoriously difficult, but German seems to drift into one

As such, the expression cited above that it may not be a recession, but it sure feels like one, is justified. In real-time early identification, quantitative approaches unfortunately do not provide timely and reliable indicators. Forecasters need to rely on as many different approaches as possible, but ultimately also to some extent on their gut feeling. They must be aware, however, that economic forecasts are based heavily on extrapolated trends and are therefore subject to a significant status quo bias. In addition, there is a risk of falling victim to confirmation bias: Once an opinion has been formed, new information is weighted by our perception in such a way that it causes as little discordance as possible to this preconceived opinion. These individual perception patterns are reinforced by group interactions with the propagation through mass media being a key factor until a tipping point has been reached. The sharp decline in the ifo and PMI surveys in January makes us believe that we might have reached such a tipping point. Even if the Statistical Office sticks to its optimistic assessment of Q4 GDP, we now expect that the German economy will shrink in Q1. A recession might then still be avoided – at least in

[5] https://www.sachverstaendigenrat-wirtschaft.de/publikationen/jahresgutachten/jahresgutachten-201819.html

technical terms. However key economic indicators have moved below trend and continue to fall, thus providing a clear indication that Germany is drifting into a recession right now.

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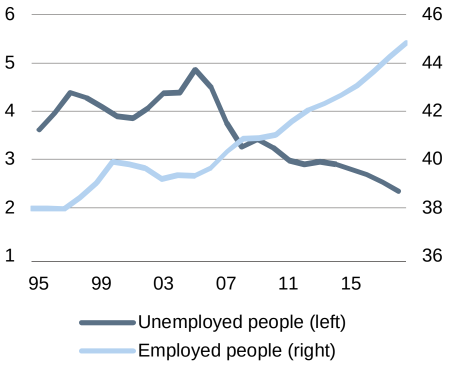
Cyclical spark does not ignite investment growth

— In 2018, investment in machinery and equipment grew by 4.5% in real terms in Germany. However, we expect this rate to slow to significantly less than 3% p.a. in 2019 and 2020 already, whereas downside risks currently predominate.

— In fact, investment in machinery and equipment has expanded at a relatively low rate during the current upswing, i.e. since 2010. The average annual rate of growth for this period is 2.7% in real terms, which is equivalent to the long-term average for the years 1995–2018. However, investment in machinery and equipment has increased at much stronger rates during other upswings since the German unification. In fact, it was up by 6.3% p.a. between 1994 and 2000 or even 6.8% p.a. between 2003 and 2008. This means that the cyclical spark has not really ignited investment growth. A stronger investment dynamic is therefore one of the missing pieces in the puzzle for a continuation of the strong upswing.

German labour market in very good shape 1

Number of unemployed and employed people in Germany, m



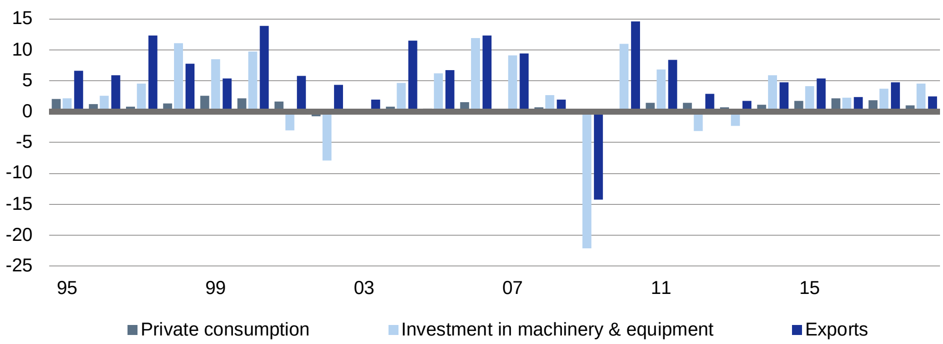
Source: Federal Statistical Office

German GDP rose for the ninth time in a row in 2018 (+1.5% in real terms according to the first estimate by the Federal Statistical Office). While the growth momentum looks set to slow further in 2019 (we expect GDP to expand by 1%), the upswing looks set to be the longest since the 1950s and 1960s.

The pattern of the current cycle is relatively atypical for Germany. Former upswings often started with a significant increase in exports. This led to higher capacity utilisation in export-oriented (and other) sectors. As a consequence, companies increased their investment in machinery and equipment. Significant employment and/or wage growth came later in the cycle, if at all. With unemployment in Germany relatively high for many years (meaning that the supply of labour was large), wage agreements in the late 1990s and in the first decade of the current century tended to be on the low side. As a consequence, private consumption was weak for a long time. In fact, foreign observers regularly remarked upon German households' low propensity to consume and called for larger wage increases, not least in order to reduce the high German trade surplus.

Growth stimuli from capital spending and exports quite small during the last few years 2

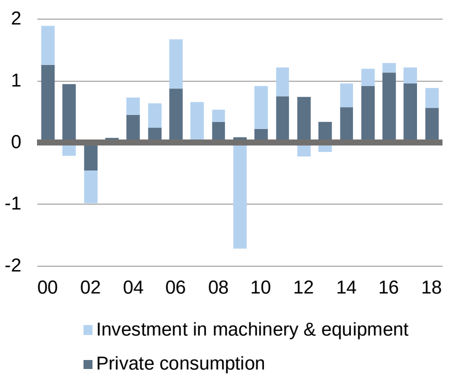
Real GDP components in Germany, % yoy



Source: Federal Statistical Office

Private consumption has been an important pillar for growth of late 3

Contribution to real GDP growth in Germany, pp



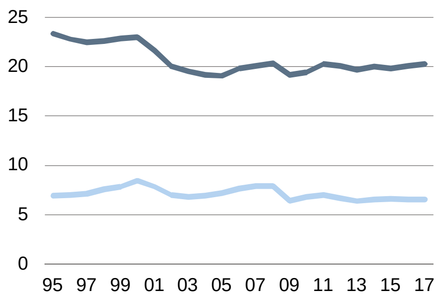
Sources: Federal Statistical Office, Deutsche Bank Research

Deviation from a typical German cycle

Contrary to this "typically German" pattern, private consumption has made a significant contribution to GDP growth since 2010, particularly in comparison to the period between 2002 and 2010. A very healthy labour market development, higher wage agreements, migration to Germany and low interest rates were major reasons behind this development. On average, private consumption has

Investment ratio relatively stable in recent years 4

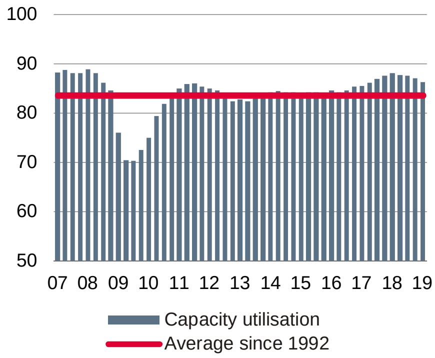
Share of investment spending in GDP in Germany (investment ratio), %



Sources: Federal Statistical Office, Deutsche Bank Research

Capacity utilisation declines slightly 5

Capacity utilisation in the manufacturing industry in Germany, %



Source: ifo Institute

grown by 1.4% p.a. in price-adjusted terms since 2010. This momentum is remarkable for Germany, seeing that the average rate of growth in private consumption was only 0.8% p.a. between 1995 and 2010.

Compared to earlier cycles, investment in machinery and equipment has grown at a relatively weak rate since 2010. During this period, it has expanded by 2.7% p.a. in real terms, which is equivalent to the long-term average for the years 1995 – 2018. However, investment in machinery and equipment has increased at much stronger rates during other upswings since the German unification. In fact, it was up by 6.3% p.a. between 1994 and 2000 or even 6.8% p.a. between 2003 and 2008. While investment in machinery and equipment was up by 4.5% in real terms in 2018, we expect the expansion to slow to significantly less than 3% p.a. in 2019 and 2020 already, whereas downside risks currently predominate. The cyclical spark is obviously not igniting investment. A stronger investment dynamic is therefore one of the missing pieces in the puzzle for a continuation of the strong upswing.

The investment ratio (i.e. the share of investment spending in aggregate GDP) was also below the long-term average between 2010 and 2017. This applies to both aggregate gross capital spending and to investment in machinery and equipment.

Investment to remain subdued for a number of reasons

A stronger rate of growth appears improbable in view of the economic and political uncertainties (Brexit, persistent trade conflicts) and the mature stage of the economic cycle. The ifo business expectations have become clearly negative. In addition, capacity utilisation in the German industry has declined over the past four quarters. While it is still above the long-term average, the downtrend suggests that capacity expansions are no longer urgently needed. The ifo manager survey of December 2018 points in this direction, too. Almost 50% of the participants plan to keep their investments unchanged in 2019 compared to 2018. While 29% intend to invest more than in 2018, 23% plan to reduce their investments in 2019 compared to 2018.

Companies have obviously learned from former crises. They had considerably increased their capital spending shortly before the “new economy” bubble burst and again in the run-up to the great economic and financial crisis of 2008/09. In both cases, they suffered from overcapacities afterwards. Companies are considerably more cautious now and invest at a slower pace than in earlier upswings.

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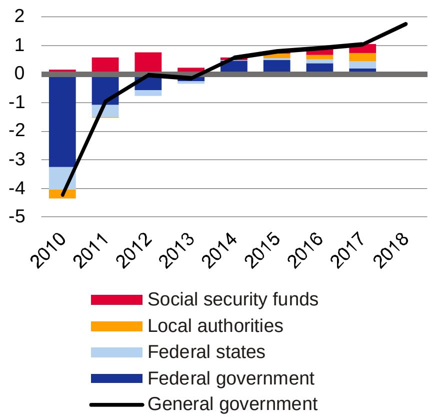
Consolidated gen. government budget surplus for the fifth consecutive year 1

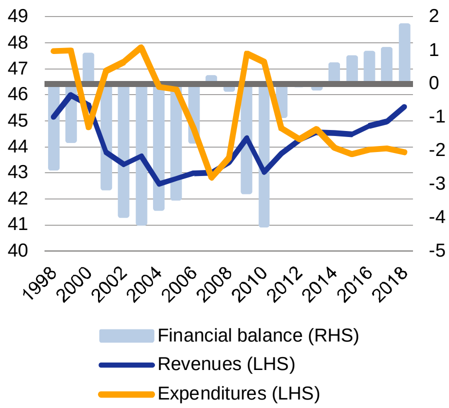
Financial balance, % GDP
(general government / national accounts)



Sources: WEFA, Destatis, Deutsche Bank Research

General government surplus with a record high surplus in 2018 2

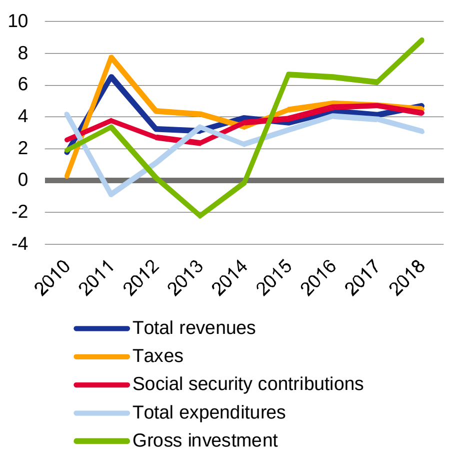
% GDP (general government / national accounts)



Sources: Destatis, Deutsche Bank Research

Revenues continued to grow more rapidly than expenditures in 2018 3

% yoy (general government / national accounts)



Sources: Destatis, Deutsche Bank Research

Record surplus despite economic downturn – does Germany need fiscal stimulus now?

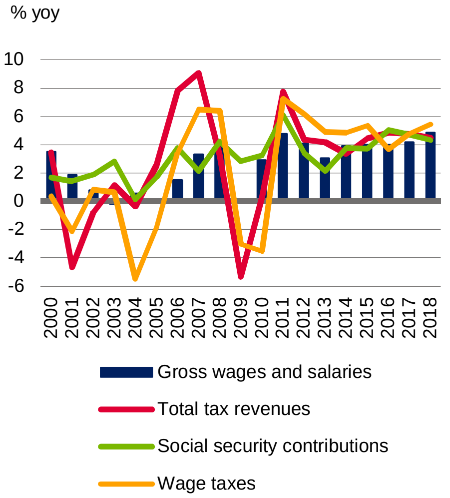
Following four years of robust, above-potential growth, GDP expanded at a considerably slower-than-expected rate of "only" 1.5% in real terms in 2018. Sluggish export demand, subdued consumption, negative one-off effects in the automotive sector and major external risks (such as increased trade tensions between the US and China, a potential no-deal Brexit, more serious debt and banking sector problems in Italy and the "yellow vest" protests in France) have made numerous economic research institutions cut their growth forecasts. We, too, have revised our forecast for 2019 downwards, from 1.3% to only 1.0%. 2019 might therefore be the first year in a long time in which GDP growth remains below the potential growth rate (of c. 1 ¼%). How will the economic downturn affect fiscal policy? And do we need fiscal stimulus, such as income tax cuts or better depreciation options (for which some policymakers and businesspeople are already calling), to stabilise growth or prevent a major downturn?

Record surplus in 2018, but the years of plenty are probably over

The slowdown has not yet affected public finances. Preliminary figures by the Federal Statistical Office (national accounts data) suggest that the general government (including special budgets), comprising the federal government, the state governments, the local authorities and the social security system, achieved an aggregate record surplus of EUR 59.2 bn (1.7% of GDP) in 2018, up from EUR 34.0 bn (1.0%) in 2017. Once again, the surplus was higher than expected (DB forecast: +1.3%). Even though detailed figures (from national accounts data) for the individual levels of government are not available yet, the (preliminary) budget surpluses for the federal government (EUR +10.9 bn) and the federal states (EUR +15.7 bn) as well as the financial results for the local authorities and the social security system up to and including Q3 2018 (financial statistics) indicate that the public surplus is broadly based.

Despite the economic slowdown, the public finances continued to benefit considerably from the favourable labour market situation (a lagging indicator for economic activity). As employment rose to a new record high of 44.8 million, (agreed) wages increased considerably and so did wage income (+4.8% after +4.2% in 2017). In turn, revenues from (wage) taxes and social security contributions continued to boom, with total tax revenues up by an aggregate 4.5% (of which wages taxes were up by 5.5%) and social security contributions by 4.3%. Low unemployment and declining interest expenses brought relief on the expenditure side of the budget. These two favourable special effects more than outweighed the (sometimes considerable) increases in spending in other fields. In addition, no nuclear fuel tax refunds took place in 2018; in 2017 they had amounted to c. EUR 7.3 bn. All in all, revenues rose by 4.7% (2017: 4.1%) and thus once again exceeded spending growth (3.1%; down from 3.8% in 2017) for the fifth year in a row. However, it is doubtful whether the trend continues in 2019, as growth weakens and the grand coalition plans (and has already adopted) additional expenditure, such as higher pensions for mothers ("Mütterrente II"), subsidies for families who want to buy a home, higher investment, defence and development support spending, more money for healthcare and old-age care etc. We believe that spending growth will once again exceed revenue growth in the future. This looks set to be a burden on the budgets in the long run.

Gross wages/salaries, tax revenues and social security contributions 4



Sources: Destatis, Deutsche Bank Research

According to the preliminary budget balance for 2018, the federal government's revenues exceeded expenditures by EUR 11.2 bn (0.3% of GDP). On that basis, the federal budget result outperformed strongly by EUR 12.8 bn (initially, the government planned – after consideration of coinage – a deficit of EUR 1.6 bn). In financial accounts terms, the federal government achieved a financial surplus of EUR 10.9 bn, which is calculated as the balance of revenue excluding revenue from coinage (c. EUR 0.3 bn) and expenditures. The federal government's structural net borrowing, which is its net borrowing adjusted for financial transactions and cyclical influences, amounted to EUR -4.8 bn or -0.15% of GDP (2017: EUR +2.7 bn or +0.09% of GDP). In other words, the federal government achieved a structural surplus. Therefore, as in the preceding years, the federal government did not need to touch the special provisions for refugees to achieve its goal of a balanced budget without new debt. In addition, the budget balance clearly stayed below the debt cap, which aims to limit structural net borrowing to a maximum of 0.35% of GDP (precise amount for the limit in 2018: EUR 11.4 bn). Under the rules of the debt brake, the cumulated differences between the upper limit for structural net borrowing and actual structural net borrowing are recorded over time on a so called control account. The overall balance rose by EUR 16.2 bn to EUR 35.1 bn in 2018.

The better-than-expected result of the federal government was due to higher-than-budgeted revenues (EUR +5.9 bn) and lower-than-expected spending (ca. EUR -6.9 bn). The higher-than-budgeted revenues were mainly driven by higher other revenues (EUR +4.8 bn) but were also partly the result of higher tax revenues (EUR +1.1 bn). The lower-than-budgeted expenditures were the result of lower interest payments (EUR -1.7 bn) as well as lower spending on labour market integration measures (EUR -1.1 bn). On top of this, investment expenditure items were lower than budgeted (EUR -1.7 bn), which was probably to some extent owing to the fact that the government had only limited fiscal elbowroom in H1 2018 due to provisional budget management. The amounts that were budgeted for investment but not fully spent are transferable and hence may be then used in future years.

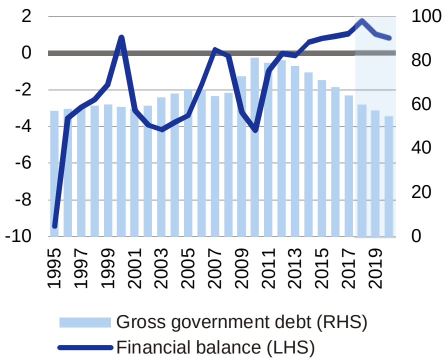
Despite the unexpected windfall only little additional fiscal leeway

Thanks to the surplus, the provisions for refugees rose to roughly EUR 35.2 bn (c. 1% of GDP or 10% of the total federal budget). According to the financial plan 2019–22, the federal government plans to withdraw roughly EUR 22.8 bn from these provisions (for example to fund the partial abolishment of the solidarity surcharge from 2021) in order to balance the budget and to ensure that the government does not take out any new debt ("black zero"). In turn, this implies that around EUR 12.4 billion (0.35% of GDP forecast for 2019) could be still at the government's free disposal for the period 2019–2022. Based on the Bundesbank's figures, which take into account the outcome of the final budget discussions in the Bundestag fiscal committee (see the monthly report for November 2018), our calculations suggest that structural net borrowing by the federal government will amount to c. EUR 8 ½ bn in 2019. This is not far below the upper limit of EUR 11 ½ bn[6]. According to this back-of-the-envelope calculation, the federal government will have a fiscal leeway of only EUR 3 bn (without accounting for the part of the provisions for refugees not yet earmarked). However, this amount is probably the lower limit, as at least part of the higher-than-expected surplus of c. EUR 12.8 bn should be structural and might therefore have a favourable "basis effect" for future budgets. In light of the

[6] Structural net borrowing is based on the budgeted structural deficit of the federal government (c. EUR 14 bn) adjusted for intended drawdowns of the refugee provision (c. EUR 5.5 bn). The structural deficit is equivalent to the budgeted core deficit of the federal government (c. EUR 6 bn) and its main special funds (c. EUR 3 bn), adjusted for a cyclical component (c. EUR 4.5 bn) and the balance of financial transactions (c. EUR 0.5 bn).

The government ran a record high surplus in 2018 - however surpluses are set to decline 5

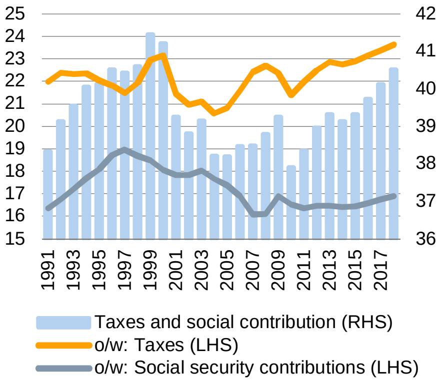
% GDP (general government / national accounts)



Sources: WEFA, Destatis, Eurostat, DB Research

Tax and contribution ratio remains high 6

% GDP (general government / national accounts)



* Taxes and social security contributions
Sources: Destatis, Deutsche Bank Research

part of the provisions not yet earmarked and the additional fiscal space for 2019 (according to the limits of the debt brake), the federal government's total fiscal leeway could be limited to around EUR 15 bn. Theoretically, the federal government could spent in addition to this already now the full amount or some parts of the provisions earmarked for future budgetary years in order to stimulate the economy. But in the above scenario this money would be missing for financing the deficits of the budgetary years to come and hence endanger the "black zero". In this context, one has to be clear that the above provisions for refugees are not held by the government as cash or deposits. Instead, these provisions simply allow the government to issue debt (credit authorisation).[7] Although withdrawals from these provisions do not have any impact on the federal government's net borrowing in terms of the government's budgetary laws, they effectively lead to an increase in debt (i.e. in the Maastricht debt stock) in the years of drawdown.

As the growth outlook and hence the budgetary prospects deteriorate, the years of fiscal plenty seem to be coming to an end. The government will have to increasingly rely on its fiscal buffers. If the government wants to respect the debt cap and keep the budget balanced, it will need to be more cautious about spending than in the past. Unexpected tax windfalls are unlikely in the near future. Now, the key question is not any more how large unexpected tax revenues may turn out to be, but whether and for how long the federal government's provisions are sufficient to fund future deficits. Still, the current macro assumptions (which do not foresee a recession!) suggest that another general government budget surplus is likely in both 2019 and 2020, even though it will probably be considerably smaller, at around 1.0% and 0.8% of GDP, respectively. Government debt (Maastricht definition) should therefore continue to decline to c. 55% of GDP by 2020 (Q3 2018: 61%).

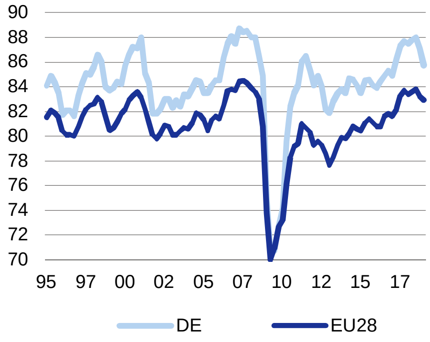
The growth engine is beginning to stutter – does Germany need fiscal stimulus?

In light of the current economic downturn policymakers are increasingly becoming nervous. The grand coalition's fiscal plans do not include a recession. Several policymakers (most of them from the CDU/CSU) have already called for tax cuts in order to prop up growth and nip a recession in the bud. The press recently speculated that the ministry of finance was preparing an "emergency plan" in case of a growth dip. And the CDU party leader recently said it was "smarter to talk about tax relief now than to prepare vague tax packages". The minister of economics underlined it was "time to stimulate growth". These statements and proposals raise the question of whether growth stimulus is indeed necessary and whether it makes sense in the current phase of the cycle. First, we should take our below-consensus growth forecast of "only" 1.0% for 2019 and compare it with potential growth and with capacity utilisation in the industry or the overall output gap. While growth might be slightly below potential in 2019, capacity overutilisation will remain in place, despite the slowdown. According to Bundesbank estimates, actual output is considerably above potential (positive output gap of c. 2%). Still, the ministry of finance believes that capacity overutilisation is considerably smaller, and what is more, such estimates are always uncertain and prone to revisions. Industrial capacity utilisation is still relatively high, at 85.7% in Q1 2019, even though it has recently declined (average since 1995: 84.1%; 2009: 72.3%). Moreover, unemployment

7 These credit authorisations did not need to be utilised because of unplanned budgetary surpluses in the previous budget years and can be used to cover deficits in subsequent years. When utilised at a later point in time, the government will have to effectively borrow money. Still, under budgetary laws these credits will not be classified as net borrowing implying that the "black zero" is achieved as long as the drawdown of these provisions is sufficient to cover any budget deficits.

EC survey: Capacity utilisation of the industrial sector has declined recently, though remains still comparatively high 7

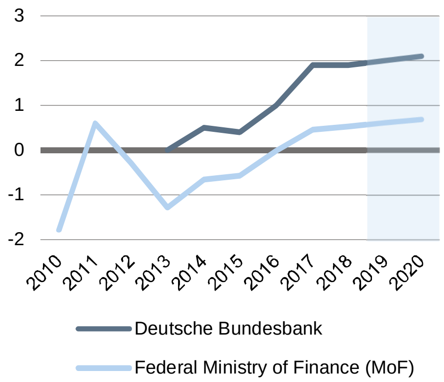
% (quarterly data) (not seasonally adjusted)



Sources: Eurostat, European Commission, Deutsche Bank Research

Estimates by the Bundesbank and the MoF point to a positive output gap 8

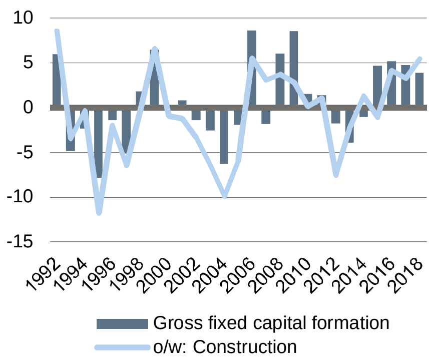
%



Sources: Deutsche Bundesbank, Ministry of Finance, Deutsche Bank Research

Real public investment 9

% yoy (general government / national accounts)



Sources: Destatis, Deutsche Bank Research

has dropped to an all-time low of 5.0% since the German unification. With the order books still full, labour market bottlenecks intensifying and supply becoming tight (particularly in construction), the slowdown looks still more like a normalisation right now. It seems quite exaggerated to call for growth packages simply because activity is normalising after a period of excessive capacity utilisation (remember, we do not expect a growth dip!). Moreover, the highly favourable structural labour market situation and the ECB's monetary policy, which will remain very expansionary for a long time to come, should continue to support growth.

Tax cuts may be a structural, but not a cyclical necessity

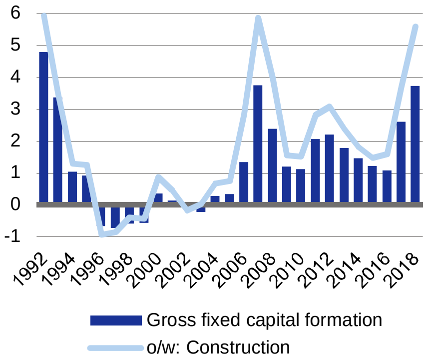
Participants in the current debate should remember that fiscal policy is already quite expansionary due to spending increases and tax cuts. According to an ifo institute estimate made in December, the fiscal stimulus will amount to EUR 24.1 bn (c. 0.7% of GDP) in 2019 alone. In 2020, expansionary measures should give the economy a boost of EUR 15.7 bn (0.4% of GDP). Apart from the increasingly expansionary and procyclical fiscal policy, there are several other arguments against providing fiscal support to the economy. In the past, experiences with growth packages ("global steering") were largely negative, not least because of the considerable time which passes between finding that growth has slowed and planning and adopting a stimulus package, which will then need additional time to have an effect. The impact of stimulus programmes is often felt when they are no longer needed. There is no reliable empirical evidence that stimulus packages have a sustained, favourable effect on long-term growth. And in case of an unexpected slump, major fiscal revenue and spending items (income tax, unemployment insurance) will stabilise growth anyway ("automatic stabilisers").

For these reasons, fiscal support does not make sense in the current phase of the cycle. Every additional euro which the government channels into the economy might simply drive prices up, but not cause output (and thus prosperity) to rise in the long run. While this applies above all to higher government spending in less productive areas, such as social security benefits, it is also true for additional investment (in digital networks or traffic infrastructure). As capacities in the construction sector, for example, are fully used, higher investment will mainly serve to push prices upwards. At least that is what the latest figures on government gross investment spending indicate. While the nominal increase was quite strong in 2018, at 7.7%, the increase in real terms amounted only to 3.8%. The gap between nominal and real growth was even larger in public-sector construction spending, for example on traffic infrastructure (11.3% vs 5.5%).

Other recent proposals, such as tax relief (for example by an earlier or complete abolishment of the solidarity surcharge and/or improved depreciation options), may make sense from a structural vantage point, for example in order to strengthen Germany's standing as a business location, improve incentives to work or boost potential growth, but are not necessary for cyclical reasons. It is remarkable that it takes a slowdown in growth to put tax cuts and relief for well-perform ng sectors of the economy on the agenda. If, however, growth slumps unexpectedly and Germany drops into a deep recession (which means that capacities would no longer be over-, but underutilised), tax cuts might be a way to prop up economic activity. However, we are still quite far away from such an unfavourable scenario. We are simply talking about a normalisation after years of exceptionally strong growth. From a cyclical vantage point, it is unnecessary to increase government spending even further. Tax relief to strengthen performance incentives and improve potential growth might make sense from a structural vantage point. However, in view of record-high government revenues

Price developments for public investment* 10

% yoy (general government / national accounts)



* calculated as the difference between nominal and real growth rates

Sources: Destatis, Deutsche Bank Research

it might make sense to fund such measures by shifts within the budget (for example by reducing unproductive spending, which weighs on fiscal sustainability).

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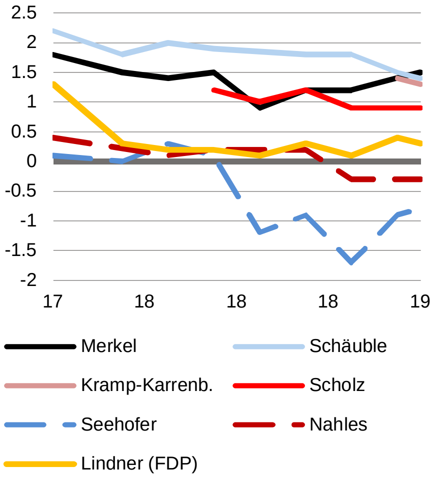
The view from Berlin

Looking beyond Brexit: German politics will heat up in the course of 2019

Major politicians' approval ratings 1

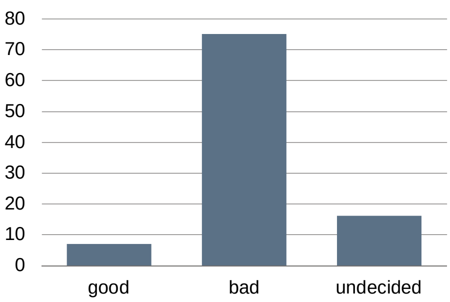
Approval rating of the respective politician on a scale from -5 to 5



Source: Forschungsgruppe Wahlen: ZDF Politbarometer

Germans' attitude regarding Brexit 2

Percentage of those surveyed



Source: Forschungsgruppe Wahlen: ZDF-Politbarometer (January 25)

Following a turbulent year in domestic politics, 2019 could become a year of consolidation, at least until the elections in east Germany in September.[8] The SPD's ambiguous attitude towards the Groko as well as bickering within the Groko, especially among CDU and CSU, proved to be disastrous for all three parties as was evident in the state elections in Hesse and Bavaria in October 2018. Therefore, the appetite for a repeat should be limited.

With Kramp-Karrenbauer's election, the CDU has set the course for gradual changes in politics. Merkel's Groko has stabilized for the time being as Kramp-Karrenbauer is unlikely to challenge the Chancellor without strong reason, Seehofer lost power and Merz virtually said goodbye to politics.

Merkel will likely focus on EU and international issues – but with limited room for manoeuvre, given the new balance of power within the CDU, i.e. between Merkel, Kramp-Karrenbauer and Brinkhaus, the CDU party whip in the Bundestag. Different views on some euro area issues between the chancellery and FM Scholz (SPD) hamper a clear positioning of Germany in further discussions in Brussels.

These differences do not prevail, though, with regard to the German government's view on Brexit. While 75% of the Germans think that Brexit is bad (Forschungsgruppe Wahlen), a similar share of people take the view that the EU should not compromise further. In line with the EU's stance on the Brexit negotiations, the German government has signalled some flexibility regarding changes to the Political Declaration which deals with the post-Brexit relationship if this were to help securing a vote of the British MPs on the Withdrawal Agreement. It is rejecting, though, an opening of the Agreement with a re-negotiation of the Irish backstop provisions itself – a demand which emerged after yet another debate in the UK parliament this week. While nothing should be ruled out in politics, it appears rather unlikely that the EU27 will accommodate PM May's pledges, in particular to allow the UK the right to exit the backstop unilaterally. It is open whether the EU will engage in further negotiations with PM May before the next meaningful vote in the UK parliament scheduled for February 13.

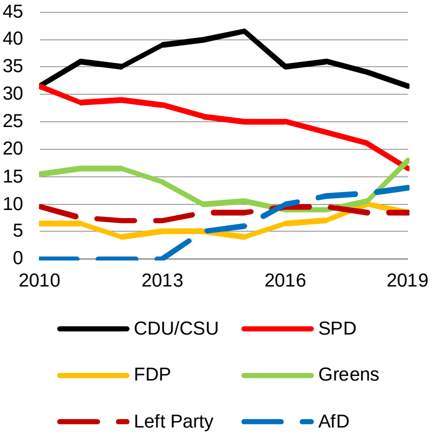
Regardless of the outcome, a short extension of Art 50 might become necessary to allow for the ratification – if there is a deal – as well as the technical implementation of legislation in any case. However, the EU Council would not decide on that before the March 21-22 summit and will likely attach conditions to it. Despite its concern over the rising risk of a no-deal Brexit and with it a further deterioration of the bilateral trade relations (nominal German exports to the UK were down in 2018 by over 7% compared with 2015), the German industry continues to back the government's consistent line.

Despite some consolidation and new leaders at the CDU's and the CSU's helm, it is unlikely Germany will resume the status quo ante as a beacon of stability, given the fragmented political landscape and a loss in economic momentum. The Groko parties' popularity rates are still meagre. This is especially true for the SPD. Its rating hit rock bottom (at about 15%) in October and has remained at this historically low level. While the CDU/CSU's rating has improved by about

[8] This article is largely based on the same titled Focus Germany Special published on January 25th, 2019.

German political parties' popularity since mid-2010 3

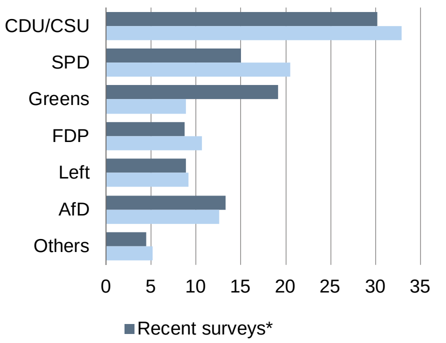
Result of the Allensbach survey, %



Source: IfD Allensbach

Major political parties' popularity & result of the last federal election 4

%



* Average of major recent surveys (Allensbach, Emnid, Forsa, Forschungsgruppe Wahlen, Infratest dimap, INSA)

Source: Wahlrecht.de (January 30)

3.5pps, it still fluctuates at about 30%, i.e. markedly below this decades' average (36%, IfD Allensbach).

The risk of political frictions or even a government crisis is likely to increase in the course of 2019, especially after May 26th with the elections for the EP and in Bremen. Later on, the state elections in Brandenburg and Saxony on September 1 and in Thuringia on October 27 will be hot spots as well. The Groko still faces a dilemma. While the parties need to strengthen their profile, renewed bickering could produce tailwinds for the AfD – an unedifying prospect for the established parties as in eastern Germany the AfD's popularity rates range between 21% to 25%, already (INSA, pmg, cf. Wahlrecht.de). Therefore, the government could be tempted to embark on even further generous social spending to please east German voters.

Debates on tax policy have already started – albeit within a questionable context. While corporate Germany hopes for substantial tax relief including better conditions for R&D investment to enhance competitiveness, recent debates have focused on the issue of distribution – as usually in Germany – and an alleged necessity of strengthening domestic demand (see article on Germany's record surplus in this issue). The conflict over tax policy is likely to intensify in the coming months, given FM Scholz' rejection of the CDU/CSU's demand for lower corporate taxes and a quick and complete abolishment of the income tax solidarity surcharge.

In contrast to some other currently debated issues such as the plan for a phase-out of coal-based energy production where – besides the energy consumers – primarily future governments (still, though, the taxpayer in general) have to take the bill for today's decisions, tax policy is more or less immediately budget relevant. Therefore, the planning and parliamentary discussion of the 2020 federal budget which will start in late March and enter a more crucial stage in early summer could result in turbulence.

Later in the year, the three state elections in east Germany will attract attention. The results of these elections will dominate the SPD's Groko midterm assessment in late autumn. Poor outcomes could result in a Groko breakup which would most likely trigger snap elections. As long as the Greens' popularity remains twice as high as their result in the last federal election and as the respective FDP rating, the Greens' interest in joining a Jamaica coalition with the CDU/CSU and the FDP in the current term as an alternative to a snap election seems to be limited.

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The R-question

Germany: Data calendar

Date	Time	Data	Reporting period	DB forecast	Last value
6 Feb 2019	8:00	New orders manufacturing (% mom, sa)	December	0.5	-1.0
7 Feb 2019	8:00	Industrial production (% mom, sa)	December	0.8	-1.8
8 Feb 2019	8:00	Trade balance (EUR bn, sa)	December	17.5	18.9
8 Feb 2019	8:00	Merchandise exports (% mom, sa)	December	-0.6	-0.3
8 Feb 2019	8:00	Merchandise imports (% mom, sa)	December	0.7	-1.3
14 Feb 2019	8:00	Real GDP (% qoq)	Q4 2018	0.1	-0.2
21 Feb 2019	9:30	Manufacturing PMI (Flash)	February	51.0	49.7
21 Feb 2019	9:30	Services PMI (Flash)	February	53.0	53.1
22 Feb 2019	10:00	ifo business climate (Index, sa)	February	100.2	99.1
22 Feb 2019	8:00	Real GDP (% qoq) - Details	Q4 2018	0.1	-0.2
28 Feb 2019	14:00	Consumer prices preliminary (% yoy, nsa)	February	1.2	1.4
1 Mar 2019	9:55	Unemployment rate (%, sa)	February	5.0	5.0
5 Mar 2019	8:00	Retail sales (% mom, sa)*	January	1.5	-4.3

*An earlier data release may be possible due to the Federal Statistical Office.
Sources: Deutsche Bank Research, Federal Statistical Office, Federal Employment Agency, ifo, Markit

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Financial Forecasts

	US	JP	EMU	GB	CH	SE	DK	NO	PL	HU	CZ
Key interest rate, %											
Current	2.375	-0.10	0.00	0.75	-0.75	-0.25	0.05	0.75	1.50	0.15	1.75
Mar 19	2.375	-0.10	0.00	0.75	-0.75	-0.25	0.05	1.00	1.50	0.20	1.75
Jun 19	2.625	-0.10	0.00	0.75	-0.75	-0.25	0.05	1.00	1.50	0.35	2.00
Sep 19	2.625	-0.10	0.00	1.00	-0.75	-0.25	0.05	1.00	1.50	0.25	2.00
3M interest rates, %											
Current	2.74	0.05	-0.31	0.92							
Mar 19	2.93	0.05	-0.35	0.80							
Jun 19	3.18	0.05	-0.33	0.90							
Sep 19	3.43	0.05	-0.30	1.05							
10Y government bonds yields, %											
Current	2.64	0.01	0.19	1.26							
Mar 19	3.00	0.10	0.45	1.50							
Jun 19	3.15	0.05	0.53	1.65							
Sep 19	3.10	0.05	0.60	1.80							
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	1.14	108.92	0.87	1.31	1.14	10.37	7.46	9.69	4.29	316.53	25.81
Mar 19	1.16	106.00	0.82	1.42	1.13	10.40		9.35	4.33	324.26	25.65
Jun 19	1.18	104.00	0.80	1.48	1.13	10.50		9.20	4.35	327.00	25.60
Sep 19	1.22	102.00	0.82	1.49	1.14	10.65		9.25	4.35	326.00	25.45

Sources: Bloomberg Finance LP, Deutsche Bank Research

German data monitor

	Q1 2018	Q2 2018	Q3 2018	Q4 2018	Q1 2019	Aug 2018	Sep 2018	Oct 2018	Nov 2018	Dec 2018	Jan 2019
Business surveys and output											
Aggregate											
Ifo business climate	104.3	102.5	103.3	102.0		104.0	103.9	102.8	102.2	101.0	99.1
Ifo business expectations	100.7	98.8	100.1	98.6		101.1	101.0	99.7	98.7	97.3	94.2
Industry											
Ifo manufacturing	107.9	105.1	104.6	101.6		105.0	104.7	102.6	101.8	100.5	98.8
Headline IP (% pop)	0.2	0.3	-1.6			0.4	-0.1	-0.6	-1.8		
Orders (% pop)	-2.6	-1.4	-1.0			2.4	0.0	0.2	-1.0		
Capacity Utilisation	88.2	87.8	87.8	87.1	86.3						
Construction											
Output (% pop)	1.3	5.8	-0.1			-1.7	4.1	-2.0	-0.8		
Orders (% pop)	0.7	-5.2	0.7			-1.4	3.7	0.4	6.1		
Ifo construction	110.2	111.6	116.6	116.9		116.6	117.7	118.0	116.4	116.3	111.6
Consumer demand											
EC consumer survey	0.7	-1.1	-1.5	-1.5		-1.2	-0.7	-1.1	-1.1	-2.3	-2.3
Retail sales (% pop)	-0.5	1.3	-0.6	0.1		-0.1	-0.3	0.8	1.6	-4.3	
New car reg. (% yoy)	4.0	1.9	1.2	-8.1		24.7	-30.5	-7.4	-9.9	-6.7	
Foreign sector											
Foreign orders (% pop)	-2.6	-1.4	-2.3			5.7	-2.0	3.0	-3.2		
Exports (% pop)	-0.4	1.0	-0.2			0.1	-0.3	0.9	-0.3		
Imports (% pop)	0.5	2.1	2.3			-2.2	0.6	0.8	-1.3		
Net trade (sa EUR bn)	61.9	59.6	52.8			18.6	17.7	17.9	18.9		
Labour market											
Unemployment rate (%)	5.4	5.2	5.2	5.0		5.2	5.1	5.1	5.0	5.0	5.0
Change in unemployment (k)	-69.3	-40.0	-35.0	-43.7		-10.0	-22.0	-11.0	-16.0	-12.0	-2.0
Employment (% yoy)	1.4	1.3	1.2	1.1		1.2	1.2	1.2	1.1	1.1	
Ifo employment barometer	104.8	103.9	104.7	104.1		105.0	104.9	104.7	103.6	104.1	103.0
Prices, wages and costs											
Prices											
Harmonised CPI (% yoy)	1.4	1.9	2.1	2.1		1.9	2.2	2.4	2.2	1.7	
Core HICP (% yoy)	1.3	1.2	1.2	1.4		1.1	1.2	1.5	1.2	1.4	
Harmonised PPI (% yoy)	2.0	2.6									
Commodities, ex. Energy (% yoy)	-12.4	2.6	-0.5	-0.3		-0.2	-2.1	1.5	-0.1	-2.2	
Crude oil, Brent (USD/bbl)	66.9	74.5	75.1	68.0		72.5	78.9	81.0	64.7	56.5	59.3
Inflation expectations											
EC household survey	16.4	17.3	21.4	21.5		21.9	21.5	21.5	21.2	21.9	20.1
EC industrial survey	15.0	13.8	15.8	17.6		15.9	16.5	14.4	17.3	21.1	18.9
Unit labour cost (% yoy)											
Unit labour cost	2.4	1.7	3.2								
Compensation	2.7	2.9	3.2								
Hourly labour costs	3.5	1.6	2.8								
Money (% yoy)											
M3	3.4	3.6	4.1	4.6		3.5	4.1	4.5	4.4	4.6	
M3 trend (3m cma)						3.6	3.8	4.0	4.3	4.5	
Credit - private	4.3	4.3	4.3	3.9		4.1	4.3	4.1	3.8	0.0	
Credit - public	-20.0	-7.0	-2.7			0.5	-2.7	-6.7	-6.4		

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

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