

Ifo index not strong enough to bring back optimism

Germany's Ifo index gives very little hope of an imminent rebound



One day before the second anniversary of Russia's invasion of Ukraine, the second estimate of fourth-quarter GDP growth has confirmed the shallow German recession in 2023, while the latest Ifo index reading gives very little hope for imminent improvement.

In more detail, the GDP components for the fourth quarter of 2023 confirmed that the economy shrank by 0.3% quarter-on-quarter. While investments were a drag on the economy, private consumption was slightly up. To put these numbers into perspective, since the start of the war in Ukraine, the German economy has been stuck in a de facto stagnation. Industrial production, meanwhile, has been mired in misery, at some 10% below pre-pandemic levels at the end of 2023. The reasons for the German weakness have been discussed endlessly and can be simply summarised as a dismal combination of cyclical headwinds and a long list of structural weaknesses.

Getting out of this vicious circle will not be easy and there are indeed very few signs of an imminent improvement. Yesterday's PMI readings were a disappointment, particularly for the manufacturing sector and this morning's Ifo index also gave very little hope of an imminent rebound. The February headline number came in at 85.5, from 85.2 in January. While the current

assessment component remained unchanged, expectations improved somewhat, albeit from very low levels. However, the near-term outlook for the German economy is not bright. Tensions in the Red Sea have led to new supply chain frictions. Strikes since the start of the year would make every Frenchman (or Frenchwoman) proud and an increasing number of insolvencies have increased the chances of yet another quarter of contraction. It is questionable whether the very few glimmers of hope, stemming from the pick-up in truck traffic on German highways or the gradual turning of the inventory cycle, are enough to prevent another economic contraction in the first quarter of 2024.

German government still in disagreement on how to support the economy

Earlier this week, the German government presented its growth forecast, which at 0.2% GDP growth for this year, is actually still above our own forecast of -0.2%. Probably even worse, the government's long-term forecasts for the economy are currently at 0.5%, finally reflecting the consequences of no policy action. While many government members were in denial last summer when the international debate about Germany being the sick man of Europe started and even earlier this year said that the economy only needed a strong coffee to wake up, the tone has changed. There now seems to be an agreement and acknowledgement of the weak state of the economy but, unfortunately, there still is disagreement on what to do. The fact that the government's decision on tax relief, which was actually taken last summer, has still not passed the Upper House and was trimmed down this week from €7bn to €3bn illustrates that the real sense of urgency is not yet very high.

All in all, data releases and political events this week confirm our view of yet another minor contraction of the German economy in the first quarter and a weak recovery thereafter.

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