German economy not out of recessionary danger, yet

The stagnation of the German economy shows that the eurozone's largest economy has not escaped the risk of a recession

Recession not yet avoided. According to a first estimate, the German economy stagnated in the first quarter of the year, following a 0.5% quarter-on-quarter contraction in the fourth quarter of last year. On the year, GDP growth was down by 0.1%. GDP components will only be released at the end of May but according to available monthly data and the statistical office's press release, growth was mainly driven by exports and activity in the construction sector, while private and public consumption were a drag on growth. After last year's experience when the economy did better than soft indicators suggested, we now have an opposite pattern, with the economy doing worse than soft indicators have suggested. Also, don't forget that in 4Q 2022, the initial estimate of a stagnating economy was revised down three times, from an initial stagnation to now -0.5% QoQ.

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Today's data shows that the warm winter weather, a rebound in industrial activity, helped by the

Chinese reopening and an easing of supply chain frictions were not enough to get the economy out of the recessionary danger zone. Private consumption continues to suffer from still-high retail energy prices.

Looking beyond the first quarter, we still think that the recent renaissance in industrial production could very well carry the economy through the second quarter. However, we are afraid that looking into the second half of the year, the German economy will continue its flirtation with recession. This is when the industrial backlog will have been reduced without new strong demand coming in, when the impact of the most aggressive monetary policy tightening in decades will fully unfold and when a slowdown of the US economy will hit German exports. On top of these cyclical factors, the ongoing war in Ukraine, ongoing demographic change and an ongoing energy transition will structurally weigh on the German economy in the coming years.

Today's GDP growth illustrates that the industrial renaissance of the last two months has not been enough to get the economy out of recessionary territory. Even though early GDP estimates have become subject to unusually strong revisions and we could still see some upward revision, the overall direction for the German economy is clear: this year will bring a long flirtation with stagnation.

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