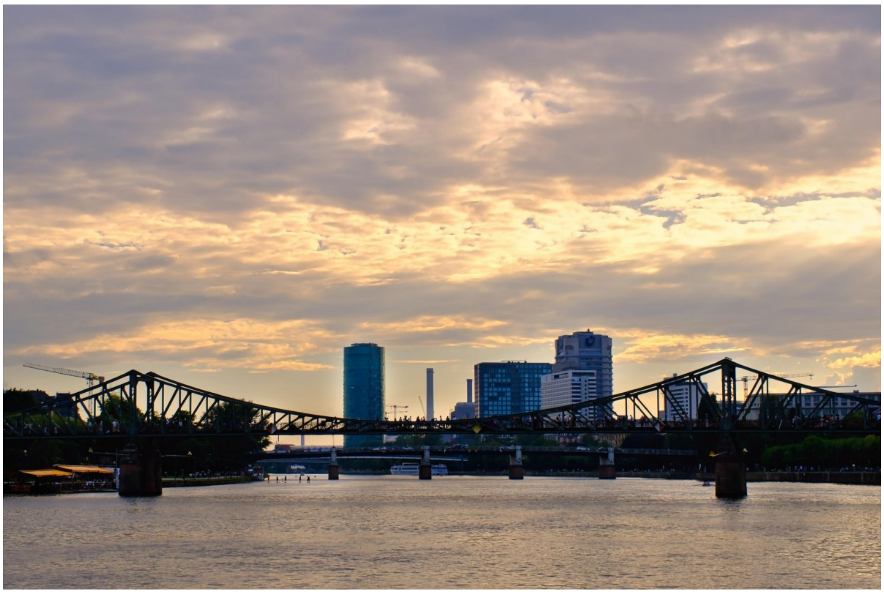
German Ifo points to a bottoming out, not a rebound in November

It's better than another drop but the latest improvement in the Ifo index is too insignificant to really celebrate. It points to a bottoming out of the German economy, rather than an imminent rebound



Germany's most prominent leading indicator, the Ifo index, increased for the second month in a row in November, coming in at 87.3, from 86.9 in October. Both the current assessment and expectations component improved somewhat. To put this increase into perspective: the Ifo index is still below its July level.

Bottoming out but fiscal woes will weigh on economy

Today's data confirms that it will not be easy for the German economy to gain fresh growth momentum. Even if the worst of the weakening in sentiment seems to be behind us, the hard economic reality does not look pretty. Be it the still-unfolding impact of the European Central Bank's monetary policy tightening, the potential slowing of the US economy or new uncertainty regarding already-announced fiscal stimulus measures, except for a turn in the inventory cycle, there doesn't seem to be a strong growth driver in sight. This is why we expect the current state of stagnation and shallow recession to continue. In fact, the risk that 2024 will be another year of recession has clearly increased. It would be the first time since the early 2000s that Germany has gone through a two-year recession, even if it proves to be a shallow one.

In the meantime, fiscal policy and the search for the missing €60bn is dominating headlines in Germany. Last night, Finance Minister Christian Lindner announced a suspension of the constitutional debt brake for the 2023 budget. Yes, the 2023 budget, not the 2024 budget. The finance ministry will now have the legal wiggle room to present a supplementary budget, which will likely include expenditures initially accounted for in off-budget vehicles.

The big debate is over the 2024 budget, which the government had wanted to conclude by the end of the year, but this is not possible now. Lindner will not agree to another emergency in 2024, which is what the Greens and the SPD are demanding. This would be political suicide for the FDP so we can confidently predict that this won't happen. This, in turn, means that the government would have to make some big savings. Subsidies are probably the least painful item to cut. More structurally speaking, the government will have to decide in the coming days and weeks whether it will structurally change the debt brake, by either calling for a multi-year suspension from the start or a reform, finding exemptions for investments, or whether it will try to fill the budgetary holes by expenditure cuts and higher taxes. The latter would clearly push the economy further into recession, leaving aside that it would lead to an unprecedented fiscal policy stance across the eurozone: austerity in a low-debt country and rather loose fiscal policies in high-debt countries.

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