

## Germany: 2019 growth down but the fiscal band plays on

A Kate-and-Leonardo or simply a Titanic moment for Germany? The economy has slowed down to the weakest level since 2013 but the fiscal balance recorded its sixth straight surplus; while the economy sinks, the fiscal band plays on



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The German statistical office just released its first estimate for annual GDP growth in 2019. The economy grew by 0.6% year-on-year, from 1.5% in 2018. This is the weakest growth rate since 2013. Don't forget that there is no single hard data available for December, yet, and that this first estimate is based on technical assumptions for December. Based on today's data, the German economy will probably have avoided stagnation in the fourth quarter.

### Still a two-faced economy

The German economy still has two faces: a strong domestic one on the back of record high employment, consumer and government spending, and a weak industrial one on the back of the global manufacturing slowdown and its sector-specific problems in the automotive industry. Up to now, strong domestic demand has offset the manufacturing slowdown. Looking into 2020, it

remains uncertain whether this balancing act can continue. In fact, in our view either the cyclical factors weighing on German industry will dissipate somewhat, with the entire economy rebounding, or the domestic part of the economy will also slow down. In our base-case scenario, global trade will rebound somewhat, and low interest rates and the weak euro should further support the export sector; just in time to avoid a significant weakening of consumption. However, structurally the economy is in worse shape than in 2008/9 or 2012/13, which will put a cap on the economy's ability to benefit from a global rebound. While growth in the 2010s looked almost effortless, it will require new reforms and investment to tackle the challenges of the 2020s.

## The sixth year in a row with a fiscal surplus

The discussion on fiscal stimulus will gain more momentum. Also this morning, the fiscal outcome for 2019 was released with the government recording yet another surplus of 1.5% GDP, from 1.9% GDP in 2018. It is the sixth consecutive year with a fiscal surplus. The last eurozone country with such a fiscal performance was Estonia in the early 2000s. The last time the German fiscal balance showed a deficit was in 2011, as 2012 and 2013 saw a balanced budget.

Contrary to what the government had previously expected, 2019 did not mark the end of the “fat years”. Instead, the economic fat years end with yet another richly-filled cash register. The political discussion in Berlin on fiscal policies has shifted away from the principal “surplus vs deficit” debate towards a debate on how to use the current surplus. There seems to be a growing political acceptance that the surplus should be used, without letting go of the ‘Black Zero’ policy (fiscal surplus). However, this discussion could re-ignite tensions in the coalition as the CDU seems to favour tax relief, while the SPD is proposing new investments.

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*All in all, today's 2019 data nicely illustrates that the fat years are over, but the cash register is still ringing.*

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In our view, short term stimulus is still not really needed. Instead, the surplus should be used to step up investment efforts in the well-known sectors: digitalisation, green deal, infrastructure and education. New investments and tax relief to support private investments, both aimed at increasing the economy's potential growth rate, could be one way forward. Either way, the new fiscal surplus, combined with changing views in the coalition parties, confirms our view that the German economy could see more fiscal stimulus than most observers expect this year and beyond.

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