Germany: Did anyone say 'recession'?

Strong private consumption and exports helped the German economy to avoid recession in the third quarter

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The German economy avoided a technical recession in the third quarter, growing by a surprising 0.1% quarter-on-quarter. At the same time, however, 2Q GDP growth was revised downwards to -0.2% quarter-on-quarter, illustrating that the economy is in a de facto stagnation. 1Q GDP growth was revised upwards to +0.5% QoQ, from +0.4% QoQ. On the year, the economy grew by 0.5% (calendar adjusted) in the third quarter. Further GDP details will only be released at the end of the month but according to available monthly data and the press statement from the German statistical office, both public and private consumption, as well as construction and exports, were the main drivers of growth. Investments were the main drag.

Recession avoided but no rebound, yet

Recession or not, the German economy has fallen into a de facto stagnation, with quarterly GDP growth averaging a meagre 0.1% QoQ since the third quarter of last year. In fact, the German economy can still be divided into two worlds: the depressive world and the happy-go-lucky one. In the depressive world, there are very few signs of an imminent bottoming or recovery of the manufacturing sector since the summer of 2018. The sector is facing and will continue to face cyclical challenges, as ongoing trade conflicts, Brexit uncertainty and slower Chinese growth, along with structural challenges, disrupt the automotive industry. In the happy-go-lucky world, private consumption remains solid on the back of low inflation, low interest rates and a still-strong labour market. The construction sector keeps on booming and the government is also inserting some fiscal stimulus. The main question, however, is how long the happy-go-lucky world can resist the negative impact from the depressive world. The latest developments suggest that the protective shield has started to crumble. Looking into 2020, it looks as if 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. Either way, don't forget that the structural challenges will not quickly and easily disappear, keeping a clear cap on any German rebound in 2020.

After 10 years of almost unstoppable economic growth, a shorter period of stagnation is not necessarily a big crisis. This also explains the resistance or at least hesitation of the German government to engage in significant short-term fiscal stimulus. Today's GDP data will do very little to change the government's position. At the same time, however, a stagnating economy, even with low unemployment and low interest rates will increase, rather than reduce wealth and income inequality. Also, contrary to the recession in 2008/2009, this time around the German economy is not structurally sound and healthy. It is in the middle of severe disruption and structural changes. In short, these challenges can either be tackled by a pro-active investment package or later with a more retrospective fiscal initiative to cushion the adverse effects from disruption.

All in all, the German economy has escaped a technical recession at the very last minute. However, despite any short-term relief, there are still very few reasons to be overly cheerful. While a growth crisis still looks unlikely, a longer period of stagnation is still in the cards.

Author

Carsten Brzeski
Global Head of Macro
carsten.brzeski@ing.de