

## Germany: Economy historically strong, politics completely uncertain

The strong 3Q growth of the German economy is confirmed while the political outlook is completely uncertain



Looking for positive news on Germany these days? Then German GDP data is what you are looking for. The German statistical agency just confirmed the strong 3Q reading for GDP growth a 0.8% QoQ, from 0.6% QoQ in 2Q. On the year, the German economy grew by 2.3%. What is new? The release of the growth components shows that net exports and investment were the main growth drivers, while private consumption and the construction sector took a break in 3Q.

The German economy continues its golden cycle. Germany's economic success story goes on and on and on. Since 2Q 2009, the German economy has grown at a quarterly average of 0.5% QoQ. Out of the last 34 quarters, only three quarters recorded negative GDP growth. The German economy is currently showing its best performance over such a long period since the mid-1990s. Even if the economy would stagnate in the final quarter of the year, GDP growth for the entire year would still come in at 2.4%; the highest reading since 2011.

## It's politics, not the economy, stupid...

In Germany, these days, it's clearly not the economy but politics which matter. Since the collapse of the coalition talks on Sunday night, political leaders and their parties have been licking their wounds and trying to find ways out of the current impasse. Political uncertainty and instability are not only new for the rest of the world but also for Germany itself.

Currently, president Steinmeier is in the lead. Eventually, he would have to be the one initiating snap elections but, first, he wants to investigate other options for a government without sending German voters to the ballot boxes again. Earlier this week, Steinmeier said that snap elections were not his first choice. Therefore, he has started and will continue until next week to investigate several other options. In our view, these options are:

1. **Grand coalition of CDU/CSU and SPD:** on paper the only feasible alternative to the so-called Jamaica coalition. However, SPD leaders this week repeated their only position that the party should stay in the opposition. Still, some pressure is built up to get the SPD to the negotiation table. While this grand coalition would be the only option left for a stable government, it would probably be political suicide for the SPD as at the next election in four years from now, very few voters will reward the SPD for having made a U-turn for the sake of the country. Normally, voters' memories don't last that long.
2. **Jamaica, after all:** President Steinmeier seems to be willing to get CDU, CSU, FDP and Greens back to the negotiation table. After all, three of the four parties involved reportedly said that sufficient compromises had been made to reach a deal. However, given personal tensions and the very special way the coalition talks ended on Sunday, a successful end to this strategy looks unlikely.
3. **Minority government:** it has never happened in Germany before, but the option of a minority government of either Merkel's CDU/CSU on its own or together with the Greens (or FDP) could be another route for Steinmeier to investigate. In a television interview, Angela Merkel said she prefers new elections over such a minority government. Also, the German political landscape is traditionally used to stable majorities. The federal system, in which regional interests sometimes conflict with national interests, also makes a construction of shifting majorities highly complicated.

All of this means that new elections in our view still look like the most likely scenario for Germany, possibly preceded by a short period of a minority government.

According to recent opinion polls, new elections would hardly change the results of the September elections. We think it is far too early to take those polls as an indicator of the outcome of any possible snap elections. And even if new elections yielded, broadly speaking, the same results as those in September, it might be the step that's needed to increase acceptance for a minority government or coalition that currently doesn't look feasible (anymore) in the eyes of leading politicians.

## Short term impact of political impasse should be limited - for Germany

In the short term, the impact from the current political impasse on the German economy should be (close to) zero. The economy has plenty of positive momentum and the external environment, including low-interest rates and the weak euro, remains favourable enough to shield the economy against political uncertainty. Also, contrary to experiences in other countries there is no risk that Germany could get a populist or unreliable government any time soon. It will only take a bit longer before a new government will be in office.

For the longer term, however, given the lack of structural reforms and the urgent need for investments in digitalization and education, German politics should not waste too much time if they don't want to put the economy's future at risk.

For Europe, the political uncertainty in Germany is bad news. Not so much for the Brexit negotiations, as here the European Commission is in the lead and the broad majority in the German parliament agrees on the stance taken so far. But for the discussions on the future of the Eurozone, also scheduled for the European Summit in December, latest developments in Germany mean that a fundamental debate will hardly be possible. The risk increases that the window of opportunity to further reform the Eurozone in economic good times could close before it was fully open.

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