Germany: Construction and government the last lines of defense

The components of 1Q GDP show that the government, the construction sector and inventories prevented a stronger contraction of the economy.

The second estimate of German GDP growth in the first quarter confirmed the sharpest drop since 1Q 2009. The German economy shrank by 2.2% quarter-on-quarter, back in 2009 it contracted by 4.7% QoQ. As the fourth quarter of 2019 was revised downwards to -0.1% QoQ, the German economy was already in a technical recession when it entered the Covid-19 crisis. On the year, the German economy contracted by 2.3%. What is new is the release of the GDP components. Private consumption fell by 3.2% QoQ, the sharpest quarterly drop since reunification. Investments dropped by almost 7% QoQ. Only government consumption (+0.2% QoQ), the construction sector (+4.1% QoQ) and inventory changes (+0.3 ppt of GDP growth) prevented a sharper contraction of the economy.

As the first quarter performance is the result of 'only' two weeks of lockdown and supply chain disruptions due to lockdown measures in Asia, it does not need much analytical skill to predict a much stronger slump in the second quarter. Three more weeks of lockdown and a very gradual lifting of some measures do not bode well for the second quarter. However, more real-time data, such as Google mobility data, shows that social and economic activity had already accelerated by mid-May. While (social and economic) activity slowed down to 60% of its January level during the peak of the lockdown, it has now returned to more than 80%. However, to offset the economic damage of the last two months, much more acceleration is needed. Therefore, it does not come as a surprise that the German government is currently preparing another fiscal stimulus package.

This morning, the leader of Angela Merkel's CDU in the German parliament, Ralph Brinkhaus, was another leading voice arguing in favour of additional fiscal stimulus, aimed at investments and increasing the economy's growth potential. We expect the government to present such a new package in the coming days. Also, Brinkhaus gave two reasons for Germany's change of heart regarding the European Recovery Fund: European solidarity and self-interest as Southern European countries were important export markets for German companies. Hard to disagree with this view.

After today's data, the first quarter of 2009 still holds the record of being the worst quarterly performance of the German economy since reunification. However, chances are high that the second quarter of 2020 will soon become the new record holder.

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