Germany: Sliding but not falling

Another drop in the Ifo index is a reason for caution but not for concern. The current assessment component is still pointing to solid growth at the start of the final quarter of the year

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Germany's most prominent leading indicator, the Ifo index, joined the choir of disappointing sentiment indicators in October, dropping to 102.8, from 103.7 in September. The decline was mainly driven by weaker expectations (from 101.0 to 99.8). The current assessment component is holding up relatively well, decreasing only marginally to 105.9, from 106.4 in September.

Stock markets, the Eurozone and the German economy, are all seeking guidance. In recent weeks, the stock market correction, the Italian fiscal conflict and a general cloud of negativism have all cast doubt about the future of the Eurozone growth cycle. At first glance, today's Ifo drop seems to add to growing concerns. However, on second glance, the German economy provides some arguments in favour of a more nuanced assessment. In fact, today's Ifo index is a perfect illustration of the current dichotomy between increasing fears about the future and solid growth at present. The high current assessment component points to continued strong growth at the start of the final quarter of the year, while weaker expectations perfectly illustrate increased worries.

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The increased worries can easily be related to the fact that the German manufacturing industry has gradually and almost unnoticed shifted one gear lower. The Ifo index for the manufacturing sector has dropped since the start of the year, while at the same time, an inventory built-up in recent months combined with less new orders doesn't bode well for industrial production in the months ahead.

Having said this, there is no reason, yet, to fall into severe depression. In fact, there is still a series of highly favourable circumstances, all being growth-supportive. Just think of low-interest rates, a weak euro and supply-side constraints. With credit growth to the corporate sector at its highest level since 2009, the domestic investment could still be the next “big growth thing”.

All of this means that the uncertainty and the unpleasant gut feeling will continue. At the same time, however, the present situation of the German economy is still better than the recent stock market correction might suggest.

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