

## Germany: Ifo stuck between vaccine and new lockdown

Don't get carried away by the stronger Ifo index. Due to the new lockdown measures, the German economy has entered a period of hibernation at the turn of the year and it will take until the second quarter before a significant rebound materialises



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Germany's most prominent leading indicator rebounded in December. The Ifo index increased to 92.1, from 90.9 in November, but still remains below the 92.5 in October. While the current assessment component improved to 91.3, from 90.0, the highest level since March, improved expectations remain clearly below summer levels.

Interpreting today's Ifo index is not easy as it was possible to fill in the survey before and after the announcement of the country's strict lockdown last Sunday. Therefore, the higher Ifo reading probably tells us more about the news and the rolling out of the vaccine, rather than the new lockdown measures.

## It will get worse before getting better

The picture of the German economy at the end of a very exceptional and unprecedented year is complicated, to say the least. Three factors are currently shaping the short-term outlook: i) after two consecutive quarters of negative impact on growth from both the construction sector and inventories, a rebound would normally be in the making. The last time the construction sector contracted three quarters in a row was 2004. ii) the manufacturing sector had a strong start to the fourth quarter, confidence remains high and order books are filled, so a contraction of the entire industry is not yet obvious. iii) the gradual tightening of restrictions up to the latest de facto shutdown of the country have led to a continuing weakening of activity in the services sector and lately also in consumption.

Expect the entire economy to go into hibernation at the turn of the year. A double dip in the fourth quarter looks inevitable, even though the strong performance of the manufacturing and construction sector up to now should make this contraction a very mild one. Looking ahead, however, it currently seems reasonable to expect an extension of the lockdown measures beyond 10 January. Given the sharp increases in new infections, an even tighter lockdown in the coming weeks can no longer be excluded. Add to this the very gradual rolling out of the vaccine and the first quarter will also be very weak. In fact, at the current juncture, a technical recession (i.e. two consecutive quarters of contraction) is also in the cards.

Before drowning in despair, the silver linings are visible. By springtime, the rolling out of the vaccine should have gained momentum and the better weather should help to significantly ease the restrictive measures and hence support the economy. Plus, the ongoing fiscal and monetary stimulus as well as an improving global economy should support and benefit the German economy throughout 2021. Hang in there. Merry Christmas.

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