

## Germany: Some balm for the soul

Finally, after six consecutive drops, the Ifo index just sent a tentative signal of relief for the German economy



Source: Shutterstock

Things can also go up. Germany's leading indicator, the Ifo index, increased in March, finally providing some evidence of a rebound. The Ifo index now stands at 99.6, up from 98.5 in February - the highest level this year. Both the expectations and the current assessment component increased. Particularly, the sharp improvement in the expectations component to 95.6, from 93.8, provides moderate optimism.

### Still in the negative sentiment loop

Looking at the bigger picture, manufacturing lost much more momentum than the services sector. Needless to say that cars play an important role in this development. The manufacturing sector has been on a downward trend since last August, dragging the entire economy down. In fact, the German economy is currently suffering from a strange and also unique combination of homemade one-off factors such as the delayed introduction of new emission standards in the automotive sector or low water levels which prevented dropping global oil prices from reaching consumers but also a series of external uncertainties. The German economy is currently the best example of how a fundamentally solid economy, with admittedly some structural flaws, can be brought to its knees by risks and uncertainties.

To paraphrase ECB president Mario Draghi's words - the German economy is somehow still caught in a dark room. A dark room, in which all of a sudden someone can easily switch on the light, and everything will be fine, or a dark room, in which the search for the exit door could still take a while.

In our view, there are currently three different trends having a stranglehold over the economy: last year's series of one-off factors, mainly impacting the automotive and chemical industry; global uncertainties like Brexit and trade; and the lack of structural reforms (including the lack of investments) over the last twenty years. None of these trends are new, and particularly regarding the lack of structural reforms, one can always only tell with hindsight whether they were curtailing growth or not.

## Bottoming out with some green shoots

Looking ahead, today's Ifo index ends a period of pessimism and suggests that not all is bad in the German economy. With some (technical) rebounds in industrial production in February and March, the first quarter for the German economy might not be as weak as some have expected.

In our view, the solid domestic fundamentals, low-interest rates and a weak euro, still argue in favour of a rebound, mainly on the back of investments, consumption and some relief from the global risk factors. At the same time, however, the risk of a self-enhancing negative sentiment loop is increasing by the month.

Fortunately, there is a non-economic leading indicator which also gives reasons for hope: the German national soccer team. Since the mid-2000s a good barometer of Germany's appetite for reforms and illustration that reforms can pay off. Just think of the impressive performance of both the national soccer team and the economy between 2010 and 2014. Over the last five years, however, since winning the World Cup title 2014, the national team has been leading the gradual decline of the German economy.

A lack of structural reforms, too much complacency and a bit of bad luck ended with an almost self-destructive depression at the end of last year. An almost complete overhaul later and a bit of good luck led to an unexpectedly positive performance last night (when the German soccer team won against the Dutch team). A bottoming out with some green shoots.

If only an overhaul of the economy was as easy as changes in the line-up of the national soccer team.

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