Germany: Return of the living dead?

Strong German growth in the first quarter suggests that any panic about the state of the eurozone's largest economy was overdone. However, there is still no room or time for complacency

Remember last year and the start of this year, when market participants and many analysts were almost speechlessly looking at the slump in German industry and the stagnating economy, giving rise to swan songs about the eurozone's largest economy and permanent downward revisions of growth forecasts for this year? The just-released GDP data for the first quarter illustrates once again that too much drama is good in movies but not necessarily in economic analysis.

The German economy grew by 0.4% quarter-on-quarter in the first quarter of the year, from 0.0% in 4Q18 and -0.2% in 2Q18. On the year, German GDP was up by 0.7%, when adjusted for seasonal and calendar effects. GDP components will only be released at the end of the month but according to available monthly data and the press release of the German statistical agency, growth was mainly driven by private consumption, investments and construction. Government spending was slightly negative.

Strong data but no time for complacency

Today’s GDP data is balm for the soul of the German economy. It also confirms our long held view that not all is bad in the German economy. Some of last year’s one-off factors have turned around, the German automotive industry might have seen better times but should not be written off and private consumption remains solid. In fact, the ongoing dichotomy between struggling industry and strong domestic demand continues and at least this time around ended with a positive outcome.

Just as weak GDP data in the second half of 2018 was not purely a result of wrong policies and business decisions or a sign that the German economic business model should be discarded, so today's strong data is no reason for complacency.

In fact, the economy still needs more investment, both from the private and public sectors, as well as new structural reforms - as much as it needed these last year and in the years before. In this regard, it remains essential that the just-started debate on more investment continues. This debate is even more important as the German economy is indeed facing several new and existing headwinds in the months ahead. The small relief from global trade and China could easily disappear and turn into even stronger headwinds if the trade war between the US and China escalates. Also, higher oil prices are likely to dent consumer spending and put additional pressure on corporate profit margins.

In our view, today's German GDP data is not necessarily the "return of the living dead" as we still see growth potential for the German economy, particularly if investments finally pick up. Instead, strong German data is rather another illustration that the condemned (often) live longer.

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