Germany: Helping hand from an old friend

December trade data shows that there are still signs of life in the eurozone's largest economy

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A more than welcome sign of life. German exports (seasonally and calendar adjusted) increased by 1.5% month-on-month in December, from 0.3% MoM in November. Imports increased by 1.2% MoM, from -1.3% MoM in November. As a result, the trade balance widened to €19.4 billion in December from €18.9 billion in November. Not adjusted for seasonal and calendar effects, exports in 2018 were some 3% higher than in 2017. Interestingly, despite all trade war fears, the export sector didn't just grow in 2018 but probably contributed positively to the economy's fourth quarter GDP growth.

What's going on in the export sector?

The German export sector was on a rollercoaster ride through all of 2018, with problems in emerging markets, trade tensions between the US and China, US protectionism, a possible cooling of the Chinese economy and increasing fears of a hard Brexit. There simply seem to be too many crises in global trade for the German export sector to defy all of them. Another factor, currently underestimated, is the exchange rate. Even though the euro remains relatively weak vis-à-vis the

US dollar, Germany's real effective exchange rate has appreciated significantly since the start of 2017 on the back of falling emerging market currencies. The currency tailwind German exporters experienced between 2015 and early 2017 has turned into a headwind. Today's data, however, shows that it is too early to give up on the German export sector.

Interestingly, when looking at the available bilateral trade data, some current assumptions are confirmed while others are actually rebutted. Despite all talk about a Chinese slowdown, the share of German exports going to China actually increased in the last few months of the year, to higher levels than the 2017 average. At the same time, despite trade war fears, the US remained the most important export destination in 2018. On the other hand, however, and not really surprising, Brexit uncertainty has left clear marks on the German export sector. While exports to the UK accounted for almost 8% of all German exports in 2015, this share has come down to 6%. If this trend continues, it would not take long before the UK has dropped out of the Top 5 of Germany's most important export partners.

Looking ahead, the balancing act for the German export sector will continue. While the temporary problems in the automotive sector will gradually be resolved (even though a WLTP 2.0 is approaching) and should boost exports, the risks and uncertainties from outside the eurozone are clearly the make-it-or-break-it factor for the export sector.

Whistling in the dark or justified optimism? Our outlook remains moderately optimistic

For the entire German economy, this week's data presents a mixed picture. While headline numbers from the industry were again disappointing, there still were some encouraging signals under the surface like the increase in new orders, excluding bulk orders, or the increase in manufacturing production. Next week's first estimate for 4Q GDP growth should still show a very small positive number.

Some might consider it whistling in the dark, but we remain modestly optimistic for the German growth outlook this year. The labour market is strong and if investment accelerates and there is some fiscal stimulus, the one-off factors which caused the slowdown in the second half of 2018 should also gradually reverse. It is not only cars but also output in the chemical industry which suffered from the low water levels in German rivers due to the dry summer as well as a sudden fall in pharmaceuticals output.

All in all, today's trade data is a welcome sign of life, confirming our view that the assessment of the German economy currently needs less black-and-white thinking and is more nuanced.

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