Germany: Still in the twilight zone

This week's German economic data in review

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While the Eurozone economy grew slightly faster than expected in the third quarter, its largest economy is still in recession risk. This week's data releases suggest that domestic demand has further weakened but is not faltering, yet.

Private consumption still holding up well

Seasonally-adjusted unemployment resumed the trend of gradual increases, witnessed throughout the entire year, in October. However, in seasonally-unadjusted terms, unemployment dropped, pushing the unemployment rate down to 4.8%, the lowest level since November 2018. At the same time, headline inflation remained unchanged at 0.9% year-on-year in October, once again bringing back memories of Mario Draghi's past comments that "with low inflation you can buy more stuff". This is exactly what German retail sales showed yesterday. Admittedly, one of the most volatile macro data but the increase in September, particularly the increase of some 0.6% quarter-on-quarter when looking at the third quarter, suggests that domestic demand should have been growth-supportive in 3Q.

Too weak to cheer but not weak enough to trigger fiscal reaction

Contraction or stagnation, the fact is that the German economy is still not weak enough for the government to react with imminent fiscal stimulus – even though the latest tax estimates, published this week, showed additional windfall revenues of some EUR4bn this year. At the same time, the latest tax estimates foresee somewhat weaker revenues in the coming four years. As a result, German public finances still offer sufficient room for manouvre.

Due to the current political situation, with SPD Finance Minister Olaf Scholz running for his party leadership and the CDU trying to defend one of the last conservative values, the Black Zero (a fiscal surplus), there is very little room for short-term stimulus. At least not in the meaning of a recession-fighting stimulus package. Obviously, the German economy also needs a longer-term investment package to improve infrastructure, digitalization and education, but the political situation makes such a package currently still unlikely.

All of this means that – in our view – there won't be any additional fiscal stimulus in Germany this year. At the earliest, after the leadership vote in the SPD (early December), the release of the 2019 GDP data (mid-January) and the January labour market data a new momentum for fiscal stimulus could emerge. In fact, while the German economy has clearly lost its glamour, it is also not performing bad enough to trigger a political reaction. Like it or not. The German economy will first have to leave the twilight zone. If it gets out as a monster, fiscal stimulus will be on the cards. If it gets out with a mild rebound, the international calls for fiscal stimulus will continue meeting deaf ears.

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