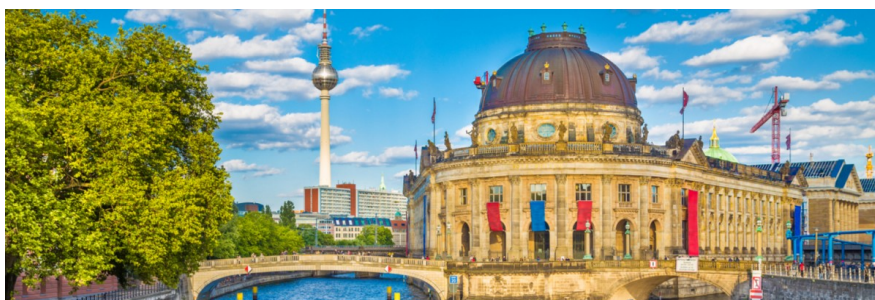


Germany: Levelling off

With its first drop since February, the German ZEW sentiment index points to a levelling off in the economy over the summer months



The latest ZEW index paints a good picture of how the recovery of the German recovery could evolve.

After the initial V-shaped recovery in May and June, a levelling off in the first summer months looks highly likely. In July, the ZEW index, which measures financial analysts' assessment and expectations of economic and financial developments, dropped for the first time since February this year, to 59.3, from 63.4 in June. At the same time, the current assessment component improved somewhat to -80.9, from -81.3 in June.

Given that traditionally, the ZEW index has a better track record in predicting turning points in the economy, rather than predicting exact outcomes for GDP growth, it is interesting to look at the difference between current assessment and expectations. This difference is currently larger than was seen in 2008 and has stabilised since May, underlining investors' optimism that the worst might be behind us.

However, even with the worst behind, today's ZEW index adds to the evidence of a levelling off in the German economy. There is also truck toll mileage data which shows that activities on German highways has returned to more than 90% of the pre-crisis level, without showing any further improvement in recent weeks.

Also, the latest announcements by some German companies to reduce employment over the next couple of years illustrates that the permanent damage from the crisis as well as the accelerated structural changes driven by the crisis will continue to leave their marks on the economy.

On a different matter, this morning's final CPI data for June showed increasing prices for food, hotels and restaurants prior to the VAT cut of 1st of July. Possibly a sign of price mark-

ups. Headline inflation came in at 0.9% month-on-month, from 0.6% MoM in May. Lower energy price limited the increase in headline inflation.

All in all, even if the ZEW index might not have the best track record in predicting actual GDP growth in Germany. This time around, it looks as if this track record will be improved - levelling off it is.

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