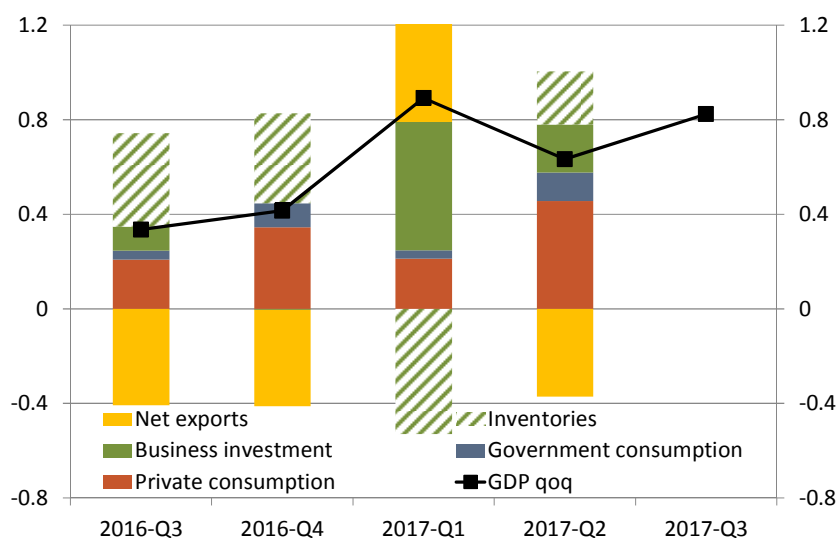


Germany: the best of the golden decade

- It will not get better than this:** While political parties jostle to form a new government, the German economy is running at full throttle. Driven by investment and exports, real GDP expanded by 0.8% qoq in Q3 according to a first estimate, after gains of 0.6% in Q2 and an upwards revised 0.9% in Q1. Taking the first three quarters of this year together, the German economy grew at the fastest annualised pace (3.2%) since 2011, thanks to strong domestic demand and a healthy cyclical upswing across the globe. We raise our calls for annual GDP growth from 2.2% to 2.5% for 2017 and from 2.0% to 2.3% for 2018, with a chance that 2017 could come in at 2.6% instead.
- Businesses seem unfazed by the run-up to the election and its aftermath.** The prospect of a fourth term of Angela Merkel suggests more of the same. Forward looking indicators such as the Ifo, which climbed to a fresh post-unification high in October, point to further solid growth in Q4 of at least 0.6% qoq. Over the course of 2018 we expect a slight slowdown in the pace of quarterly growth to 0.5% qoq.
- Strong exports:** Germany's statistical office provided only a qualitative assessment of the GDP drivers today. A quantitative breakdown will be published on 23 November. According to Destatis, economic activity accelerated on the back of firm gains from capital investment, especially in equipment, and external trade. Having contributed strongly to the expansion of demand in the previous quarters, private and public consumption took a breather in Q3, remaining largely unchanged.
- Positive outlook for consumption:** Strong employment gains are driving increases in households' disposable income, confidence and spending. Wage gains are also starting to tick up as labour demand is expanding by more than supply. Vacancies at 760,000 hit a new high in October. In addition, private consumption continues to benefit from policy measures such as modest income tax cuts at the beginning of 2017. Further measures to boost households' purchasing power are likely to come in the next couple of years. The government's consumption remained fairly flat from Q2, according to the press release. With more parties than before likely to be part of the government, and in a position to deliver on some of their campaign proposals, government expenditure will likely rise substantially.

Chart: Contributions to German GDP growth (qoq, in percentage points)



Source: Destatis

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- Business investment up strongly:** Despite a correction in September, German industrial production was up by 1.1% in Q3 compared to Q2, when it expanded by an even stronger 1.7%. Germany's major trading partners, the rest of the Eurozone, the US and emerging markets, enjoy a solid upswing. The broader and firmer recovery encourages German businesses to expand their production capacity. At a utilisation rate of 87.1% among manufacturers according to the Ifo October survey and compared to a long-term average of 83.7%, this is hardly a surprise. Investment in higher production capacities bodes well for Germany's long-term growth.
- Trade adds to growth in Q3:** Stronger foreign demand and a stabilisation in the exchange rate since early August have more than offset the impact of the euro's appreciation by up to 12% versus the US dollar since the beginning of this year. Looking ahead, we expect imports to rise faster than exports. German households are in a favourable position to consume more Spanish ham, French wine and Italian cheese. Non-Eurozone imports have also increased as the stronger euro has made it cheaper for Germans to travel to the UK, the US and elsewhere. Over time, this will narrow the current account surplus and rebalance the economy away from foreign demand and more towards domestic demand.

Table: German economic forecasts

		2016	2017	2018	2019	1Q17	2Q17	3Q17	4Q17	1Q18	2Q18	3Q18	4Q18	1Q19	2Q19	3Q19	4Q19
GDP ¹	% y/y	1.9	2.5	2.3	1.9	2.1	2.3	2.8	3.0	2.6	2.4	2.1	2.0	1.9	1.9	1.9	1.9
	% q/q					0.9	0.6	0.8	0.6	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.5
	%q/q ann.					3.6	2.6	3.3	2.4	2.0	2.0	1.9	1.9	1.9	1.9	1.9	1.9
Private Consumption	% y/y	1.9	2.0	2.0	2.0	1.6	2.2	2.2	2.1	2.2	1.9	2.0	1.9	2.0	2.0	2.0	2.0
	% q/q					0.4	0.8	0.3	0.6	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.5
Government Consumption	% y/y	3.7	1.6	1.9	2.0	1.6	1.5	1.6	1.6	1.9	1.8	2.0	2.0	2.0	2.0	2.0	2.0
	% q/q					0.2	0.6	0.3	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.5
Investment	% y/y	2.9	4.2	3.7	3.3	2.0	4.3	4.8	5.8	3.9	3.8	3.6	3.5	3.4	3.3	3.2	3.2
	% q/q					2.7	1.0	1.0	0.9	0.9	0.9	0.9	0.8	0.8	0.8	0.8	0.8
Final Domestic Demand ²	% y/y	2.4	2.4	2.4	2.3	1.7	2.5	2.6	2.8	2.5	2.3	2.4	2.3	2.3	2.3	2.3	2.3
	% q/q					0.8	0.8	0.7	0.7	0.7	0.7	0.7	0.7	0.7	0.7	0.7	0.7
Net Exports ²	% y/y	-0.4	0.2	-0.1	-0.2	0.5	-0.6	0.2	0.5	-0.1	0.2	-0.2	-0.3	-0.3	-0.3	-0.2	-0.2
	% q/q					0.6	-0.4	0.3	0.0	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1
Stockbuilding ²	% y/y	-0.1	0.1	0.2	0.0	0.0	0.5	0.2	-0.2	0.4	0.1	0.1	0.1	0.0	0.0	0.0	0.0
	% q/q					-0.5	0.2	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Current Account Balance	EUR bn	258	248	231	213	64	59	68	57	60	56	63	52	55	51	59	48
	% of GDP	8.2	7.6	6.9	6.1	8.1	7.3	8.2	6.9	7.2	6.7	7.4	6.1	6.5	5.9	6.6	5.4
Industrial Production ³	% y/y	1.0	2.7	1.5	1.7	1.0	3.0	4.0	2.9	2.5	1.2	0.5	1.7	1.6	1.7	1.7	1.7
	% q/q					0.9	1.7	1.1	-0.8	0.5	0.4	0.4	0.4	0.4	0.4	0.4	0.4
Unemployment Rate ⁴	%	4.2	3.7	3.6	3.8	3.9	3.8	3.6	3.6	3.6	3.6	3.6	3.7	3.8	3.8	3.8	3.8
CPI ⁵	% y/y	0.4	1.7	1.7	1.8	1.9	1.6	1.7	1.7	1.6	1.7	1.9	1.6	1.7	1.8	1.9	1.9
General Govt. Balance	% of GDP	0.8	1.0	0.7	0.5												
General Govt. Debt	% of GDP	68.1	64.4	61.5	58.6												

¹ Calendar-adjusted ² Contribution to GDP growth ³ Ex construction, s.a., period averages ⁴ ILO measure, period averages, s.a.

⁵ EU-harmonised, period averages

Source: Berenberg calculations

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Contacts



BERENBERG

PARTNERSHIP SINCE 1590

JOH. BERENBERG, GOSSLER & CO. KG

Internet www.berenberg.com

E-mail: firstname.lastname@berenberg.com

EQUITY RESEARCH

AEROSPACE & DEFENCE
 Ryan Booker +44 20 3753 3074
 Andrew Gollan +44 20 3207 7891
 Charlotte Keyworth +44 20 3753 3013
 Ross Law +44 20 3465 2692

AUTOMOTIVES

Cristian Dirpes +44 20 3465 2721
 Alexander Haissl +44 20 3465 2749
 Fei Teng +44 20 3753 3049

BANKS

Adam Barrass +44 20 3207 7923
 Stephanie Carter +44 20 3207 3106
 James Chappell +44 20 3207 7844
 Michael Christodoulou +44 20 3207 7920
 Andrew Lowe +44 20 3465 2743
 Andreas Markou +44 20 3753 3022
 Alex Medhurst +44 20 3753 3047
 Eoin Mullany +44 20 3207 7854
 Peter Richardson +44 20 3465 2681

BEVERAGES

Javier Gonzalez Lastra +44 20 3465 2719
 Matt Reid +44 20 3753 3075

BUSINESS SERVICES, LEISURE & TRANSPORT

Roberta Ciaccia +44 20 3207 7805
 Najet El Kassir +44 20 3207 7836
 William Fitzalan Howard +44 20 3465 2640
 Stuart Gordon +44 20 3207 7858
 Annabel Hay-Jahans +44 20 3465 2720
 Josh Puddle +44 20 3207 7881
 Kate Somerville +44 20 3753 3081
 Joel Spungin +44 20 3207 7867

CAPITAL GOODS

Nicholas Housden +44 20 3753 3050
 Sebastian Kuenne +44 20 3207 7856
 Philippe Lorrain +44 20 3207 7823
 Rizk Maidi +44 20 3207 7806
 Jaroslav Pominkiewicz +44 20 3753 3035
 Simon Toennesen +44 20 3207 7819
 Ethan Zhang +44 20 3465 2634

EQUITY SALES

SPECIALIST SALES

AEROSPACE & CAPITAL GOODS
 Cara Luciano +44 20 3753 3146

AUTOS & TECHNOLOGY

Edward Wales +44 20 3207 7815

BANKS, DIVERSIFIED FINANCIALS & INSURANCE

Iro Papadopoulou +44 20 3207 7924
 Calum Marris +44 20 3753 3040

BUSINESS SERVICES, LEISURE & TRANSPORT

Rebecca Langley +44 20 3207 7930

CONSTRUCTION, CHEMICALS, METALS & MINING

James Williamson +44 20 3207 7842

CONSUMER DISCRETIONARY

Victoria Maigrot +44 20 3753 3010

CONSUMER STAPLES

Molly Wylenzek +44 20 3753 3064

HEALTHCARE

David Hogg +44 20 3465 2628

MEDIA & TELECOMMUNICATIONS

Julia Thanheiser +44 20 3465 2676

THEMATICS

Chris Armstrong +44 20 3207 7809

SALES

BENELUX

Miel Bakker +44 20 3207 7808
 Bram van Hijfte +44 20 3753 3000

GERMANY

Michael Brauburger +49 69 91 30 90 741
 Nina Buechs +49 69 91 30 90 735
 André Grosskurth +49 69 91 30 90 734
 Florian Peter +49 69 91 30 90 740
 Joerg Wenzel +49 69 91 30 90 743

UK (cont'd)

Fabian De Smet +44 20 3207 7810

CHEMICALS

Sebastian Bray +44 20 3753 3011
 Rikin Patel +44 20 3753 3080

CONSTRUCTION

Saravana Bala +44 20 3753 3043
 Zaim Beekawa +44 20 3207 7855
 Lush Mahendrarajah +44 20 3207 7896
 Robert Muir +44 20 3207 7860
 Olivia Peters +44 20 3465 2646

DIVERSIFIED FINANCIALS

Chris Turner +44 20 3753 3019
 Michelle Bendit +44 20 3465 2729

FOOD MANUFACTURING AND H&PC

Rosie Edwards +44 20 3207 7880
 Philip Patricia +44 20 3753 3039
 Fintan Ryan +44 20 3465 2748
 James Targett +44 20 3207 7873

FOOD RETAIL

Dusan Milosavljevic +44 20 3753 3123

GENERAL MID CAP - DACH

Gunnar Cohrs (DACH + US) +44 20 3207 7894
 Martin Comtesse +44 20 3207 7878
 Charlotte Friedrichs +44 20 3753 3077
 Gustav Fröberg +44 20 3465 2655
 Julia Kochendörfer +44 20 3753 3052
 Gerhard Orgonas +44 20 3465 2635
 Henrik Paganetty +44 20 3453 3140
 Benjamin Pfannes-Varrow +44 20 3465 2620
 Julia Scheuffer +44 20 3753 3016

GENERAL MID CAP - EU core

Amyeric Lang +44 20 3753 3037
 Anna Patrice +44 20 3207 7863
 Trion Reid +44 20 3753 3113

GENERAL MID CAP - UK

Joseph Barron +44 20 3207 7828
 Calum Battersby +44 20 3753 3118
 Robert Chantry +44 20 3207 7861

UK (cont'd)

Jules Emmet +44 20 3753 3260
 Robert Floyd +44 20 3753 3018
 Karl Hancock +44 20 3207 7803
 Sean Heath +44 20 3465 2742
 James Hunt +44 20 3753 3007
 Gursumeet Jhaji +44 20 3753 3041
 James McRae +44 20 3753 3036
 David Mortlock +44 20 3207 7850
 Eleni Papoula +44 20 3465 2741
 Bhavin Patel +44 20 3207 7926
 Kushal Patel +44 20 3753 3038
 Richard Payman +44 20 3207 7825
 Christopher Pyle +44 20 3753 3076
 Joanna Sanders +44 20 3207 7925
 Mark Sheridan +44 20 3207 7802
 George Smibert +44 20 3207 7911
 Alexander Wace +44 20 3465 2670
 Paul Walker +44 20 3465 2632

FRANCE

Thibault Bourgeat +33 1 5844 9505
 Alexandre Chevassus +33 1 5844 9512
 Dalila Farigoule +33 1 5844 9510

SCANDINAVIA

Mikko Vanhala +44 20 3207 7818
 Marco Weiss +49 40 350 60 719

SWITZERLAND, AUSTRIA & ITALY

Andrea Ferrari +41 44 283 2020
 Gianni Lavigna +41 44 283 2038
 Jamie Nettleton +41 44 283 2026
 Yannick Rath +41 44 283 2029

CRM

Laura Cooper +44 20 3753 3065

GENERAL MID CAP - UK (cont'd)

Sam England +44 20 3465 2687
 Ned Hammond +44 20 3753 3017
 Omar Ismail +44 20 3753 3102
 Ian Osburn +44 20 3207 7814
 Antony Plom +44 20 3207 7908
 Edward James +44 20 3207 7811
 Benjamin May +44 20 3465 2667
 Owen Shirley +44 20 3465 2731
 Donald Tait +44 20 3753 3031

GENERAL RETAIL

Conrad Bartos +44 20 3753 3053
 Michelle Wilson +44 20 3465 2663

HEALTHCARE

Scott Bardo +44 20 3207 7869
 Jakob Berry +44 20 3465 2724
 Alistair Campbell +44 20 3207 7876
 Klara Fernandes +44 20 3465 2718
 Tom Jones +44 20 3207 7877
 Joseph Lockey +44 20 3465 2730
 Michael Ruzic-Gauthier +44 20 3753 3128
 Laura Sutcliffe +44 20 3465 2669
 Charles Weston +44 20 3465 2746

INSURANCE

Trevor Moss +44 20 3207 7893
 Emanuele Musio +44 20 3207 7916
 Iain Pearce +44 20 3465 2665

LUXURY GOODS

Mariana Horn +44 20 3753 3044
 Lauren Molyneux +44 20 3207 7892
 Zuzanna Pusz +44 20 3207 7812

MEDIA

Robert Berg +44 20 3465 2680
 Laura Janssens +44 20 3465 2639
 Alastair Reid +44 20 3207 7841
 Sarah Simon +44 20 3207 7830

REAL ESTATE

Kai Klöse +44 20 3207 7888
 Tina Munda +44 20 3465 2716

CRM

Jessica Jarmyn +44 20 3465 2696
 Madeleine Lockwood +44 20 3753 3110
 Rita Pilar +44 20 3753 3066

COO Office

Greg Swallow +44 20 3207 7833
 Fenella Neill +44 20 3207 7868

CORPORATE ACCESS

Lindsay Arnold +44 20 3207 7821
 Jennie Jirjiny +44 20 3207 7886
 Ross Mackay +44 20 3207 7866
 Stella Siggins +44 20 3465 2630
 Lucy Stevens +44 20 3753 3068
 Abbie Stewart +44 20 3753 3054

EVENTS

Charlotte David +44 20 3207 7832
 Suzy Khan +44 20 3207 7915
 Natalie Meech +44 20 3207 7831
 Eleanor Metcalfe +44 20 3207 7834
 Rebecca Mikowski +44 20 3207 7822
 Ellen Parker +44 20 3465 2684
 Sarah Weyman +44 20 3207 7801

SALES TRADING

HAMBURG
 Tim Storm +49 40 350 60 415

PARIS

Vincent Klein +33 1 58 44 95 09
 Antonio Scutto +33 1 58 44 95 03

LONDON

Assia Adanouj +44 20 3753 3087
 Charles Beddow +44 20 3465 2691

METALS & MINING

Charlie Clark +44 20 3207 3133
 Fawzi Hanano +44 20 3207 7910
 Michael Stoner +44 20 3465 2643
 Yuriy Vlasov +44 20 3465 2674

TECHNOLOGY

Josep Bori +44 20 3753 3058
 Georgios Kertsos +44 20 3465 2715
 Tej Sthankiya +44 20 3753 3099
 Gordon Tveito-Duncan +44 20 3753 3100
 Tammy Olu +44 20 3465 2673

TELECOMMUNICATIONS

Ondrej Cabejsk +44 20 3753 3071
 Nicolas Didio +44 20 3753 3091
 Usman Ghazi +44 20 3207 7824
 Siyi He +44 20 3465 2697
 Laura Janssens +44 20 3465 2639

THEMATIC RESEARCH

Nick Anderson +44 20 3207 7838
 Oyvind Bjerke +44 20 3753 3082
 Steven Bowen +44 20 3753 3057
 Asad Farid +44 20 3207 7932
 Robert Lamb +44 20 3465 2623
 Paul Marsch +44 20 3207 7857
 Saliha Sharif +44 20 3753 3097
 James Sherborne +44 20 3753 3073

TOBACCO

Jonathan Leinster +44 20 3465 2645

UTILITIES

Oliver Brown +44 20 3207 7922
 Andrew Fisher +44 20 3207 7937
 Neha Saxena +44 20 3753 3048
 Lawson Steele +44 20 3207 7887

ECONOMICS

Florian Hense +44 20 3207 7859
 Carsten Hesse +44 20 3753 3001
 Kallum Pickering +44 20 3465 2672
 Holger Schmieding +44 20 3207 7889

LONDON (cont'd)

Mike Berry +44 20 3465 2755
 Joseph Chappell +44 20 3207 7885
 Stewart Cook +44 20 3465 2752
 Mark Edwards +44 20 3753 3004
 Tom Floyd +44 20 3753 3136
 Tristan Hedley +44 20 3753 3006
 Peter King +44 20 3753 3139
 Simon Messman +44 20 3465 2754
 AJ Pulley +44 20 3465 2756
 Matthew Regan +44 20 3465 2750
 Michael Schumacher +44 20 3753 3006
 Paul Somers +44 20 3465 2753

EQUITY TRADING

HAMBURG

David Hohn +49 40 350 60 761
 Gregor Labahn +49 40 350 60 571
 Lennart Pleus +49 40 350 60 596
 Marvyn Schweden +49 40 350 60 576
 Omar Sharif +49 40 350 60 563
 Philipp Wichmann +49 40 350 60 346
 Christoffer Winter +49 40 350 60 559

LONDON

Edward Burlinson-Rush +44 20 3753 3005
 Richard Kenny +44 20 3753 3083
 Chris McKeand +44 20 3207 7938
 Ross Tobias +44 20 3753 3137

ELECTRONIC TRADING

Jonas Doehler +44 40 350 60 391
 Matthias Führer +49 40 350 60 597
 Sven Kramer +49 40 350 60 347
 Matthias Schuster +44 40 350 60 463

BERENBERG CAPITAL MARKETS LLC

Member FINRA & SIPC

E-mail: firstname.lastname@berenberg-us.com

EQUITY RESEARCH

Andrew Fung +1 646 445 5577
 Adam Mizrahi +1 646 445 4878
 Gal Munda +1 646 445 4846

EVENTS

Laura Hawes +1 646 445 4849

CORPORATE ACCESS

Olivia Lee +1 646 445 7212
 Tiffany Smith +1 646 445 4874

EQUITY SALES

SALES
 Enrico DeMatt +1 646 445 4845
 Kelleigh Faldi +1 617 292 8288
 Ted Franchetti +1 646 445 4864
 Shawna Giust +1 646 445 7216
 Rich Harb +1 617 292 8228
 Zubin Hubner +1 646 445 5572
 Michael Lesser +1 646 445 5575
 Jessica London +1 646 445 7218
 Anthony Masucci +1 617 292 8282
 Ryan McDonnell +1 646 445 7214

SALES (cont'd)

Emily Mouret +1 415 802 2525
 Peter Nichols +1 646 445 7204
 Kieran O'Sullivan +1 617 292 8292
 Rodrigo Ortigao +1 646 445 7202
 Rammigro Sroa +1 415 802 2523
 Matt Waddell +1 646 445 5562

CRM

LaJada Gonzales +1 646 445 7206
 Monika Kwok +1 646 445 4863

SALES TRADING

Ronald Cestra +1 646 445 4839
 Michael Haughey +1 646 445 4821
 Christopher Kanian +1 646 445 5576
 Lars Schwartau +1 646 445 5571
 Brett Smith +1 646 445 4883
 Bob Spillane +1 646 445 5574
 Jordan White +1 646 445 4858

ECONOMICS

Mickey Levy +1 646 445 4842
 Roiana Reid +1 646 445 4865