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MORE HOPE: GERMAN IFO BUSINESS EXPECTATIONS STABILISE

Berenberg Macro Flash

German Ifo, June

	Business climate	Expectations	Current assessment
Actual:	101.8	98.6	105.1
Previous:	102.3	98.6	106.1
Consensus:	101.8	98.0	105.6
Berenberg:	101.8	98.1	105.6

Another ray of hope: For the seventh month in a row business sentiment in Germany cooled. The Ifo's gauge of business climate fell from 102.3 in May to 101.8 in June, the lowest level since May 2017 (see chart 1). Both major sectors, manufacturing and services, suffered losses (see chart 2). Contrary to last week's German PMI, the Ifo's subindex for the service sector did not improve. The drop in the headline climate index was driven by a weaker assessment of the current situation – another nod that the exceptionally good times of H2 2017 are definitely over. Still, there is some hope that the past months' rot could also be over. Interestingly, the forward-looking sub-index of business expectations held steady in June for the first time in seventh month after stabilising already in May (see chart 1).

Based on 9000 responses from businesses in services (50.5%), manufacturing (30.2%), trade (13.3%) and construction (6%) the Ifo survey represents a large part of the German economy. The Ifo index traces the course of German GDP closely – the correlation with the quarterly growth rate is 54.3% and with the annual growth rate 85.4%. The Ifo survey is, therefore, one of the – if not the – most important gauge(s) for the German economy.

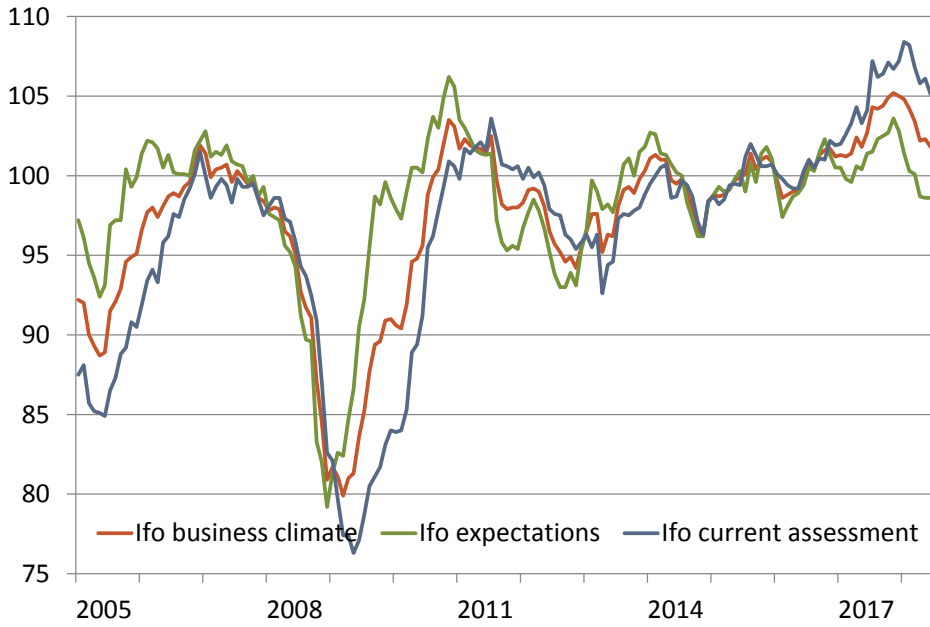
Getting used to the protectionist noise: Over the course of 2018 Ifo business expectations have fallen close to their long-term average since 2005 (98.6 vs. 98.3). Trade tensions have left their mark on the export-oriented German economy. The German economy depends more than almost any other on free trade. Turning away from free trade would be expensive for the German economy. A recent intensification of those tensions also does not help. Uncertainty about the outlook continues and sentiment is unlikely to improve significantly throughout the summer. Yet, the stable business expectations in June suggest that we may observe firms starting to get used to the protectionist noise and turn to business (almost) as usual – either because firms look more inward at a strong domestic economy, realise that export orders, including from the US, hold up or Trump may surprise all by striking deals after all. [The trade war risk, though, is not negligible.](#)

German upswing remains intact. The further strengthening labour market continues to support a solid increase in disposable incomes and consumption. While higher energy prices are putting a temporary strain on private consumption, from autumn onwards the economy should regain momentum, as also Q1's exceptional factors (weather, flu, no government, stronger euro) correct. After a quarterly growth rate of 0.3% in Q1, we expect the economy to expand at a rate of 0.5% during Q2 and Q3, before accelerating to 0.6% in Q4. From 2019 onwards, supply will likely constrain demand growth to rates which are lower, but still healthy and above trend from 2019 (0.4-0.5%).



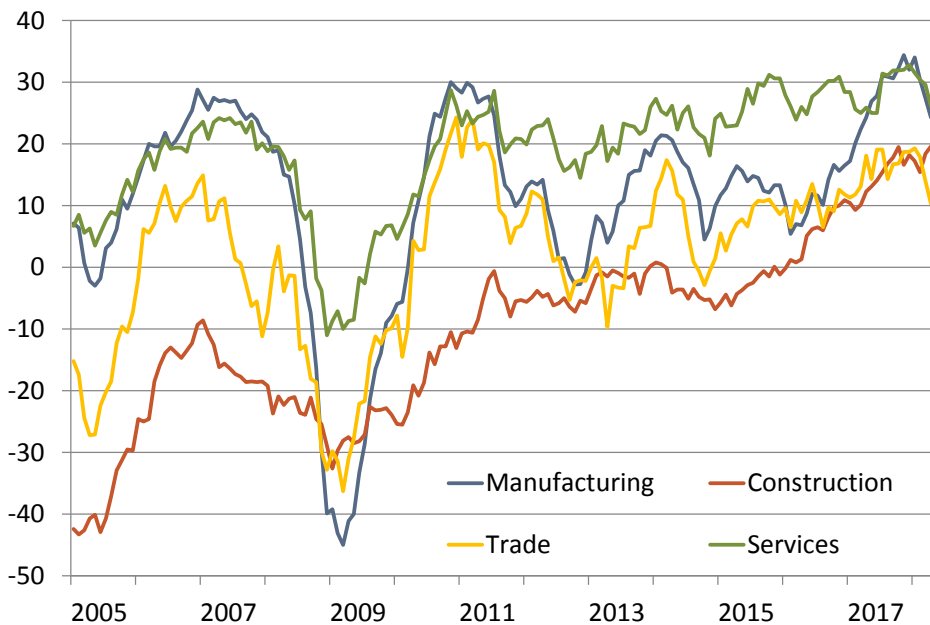
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Chart 1: Ifo business climate, current assessment and expectations



Source: Ifo

Chart 2: Ifo business climate by sector



Source: Ifo



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