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GERMAN IFO: THE BAD NEWS KEEP COMING IN

Berenberg Macro Flash

German Ifo, July

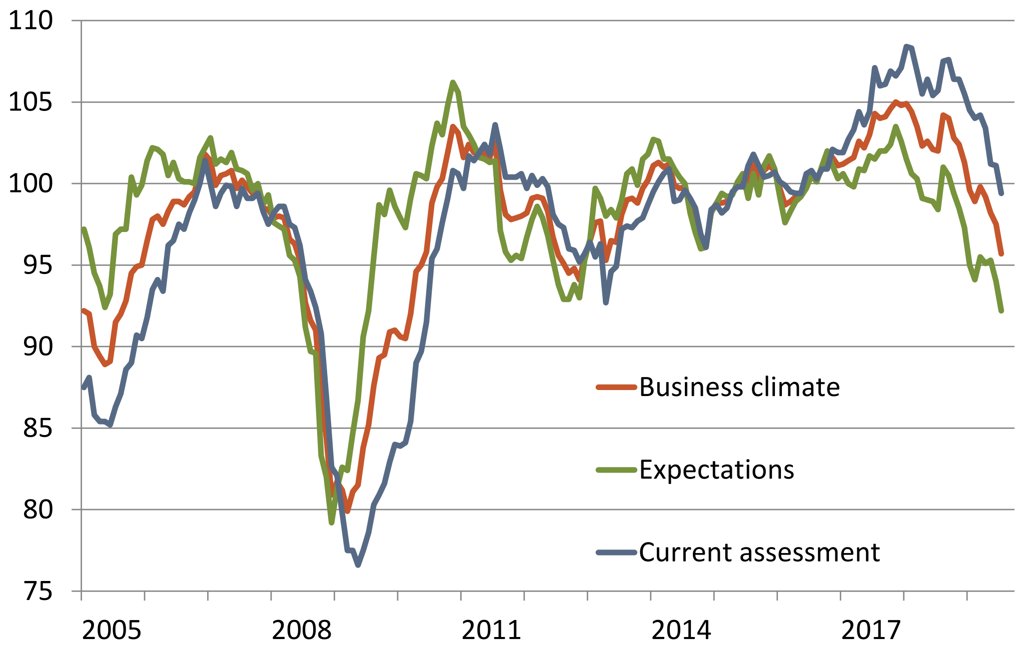
	Business climate	Expectations	Current assessment
Actual:	**95.7**	**92.2**	**99.4**
Previous:	97.4	94.2	100.8
Consensus:	97.2	94.0	100.4
Berenberg:	97.2	94.0	100.4

From bad to worse: Germany's most reliable leading indicator suffered the biggest hit in July since April 2013. The Ifo survey business climate index fell for the fourth consecutive month, with declines across the board (see Chart 1 and 2). Businesses downgraded their assessment of both the current situation and future prospects. In line with the July PMIs published yesterday, manufacturers were hid hardest – reporting the weakest assessment since October 2012. But the climate also softened among domestically-orientated services and trade. This suggests that the external weakness is spilling over to the domestic economy – which had held up nicely for a while – more than before.

ECB – worse than just "absence of improvement": The weak German Ifo strengthens the case for the ECB to cut rates – and perhaps step up QE too – today already rather than wait until September. However, for now we expect the ECB to remain on hold and instead send a strong signal via its guidance that it will act soon. The ECB usually waits for big policy changes for updated forecasts which are only due at the next meeting. We think today is about talking (guidance tweaks) and September about walking (policy change). To address the latest economic weakness and increased market expectations of a policy change, ECB president Mario Draghi may reveal that the Governing Council has tasked the relevant committees to investigate options for a re-launch of QE.

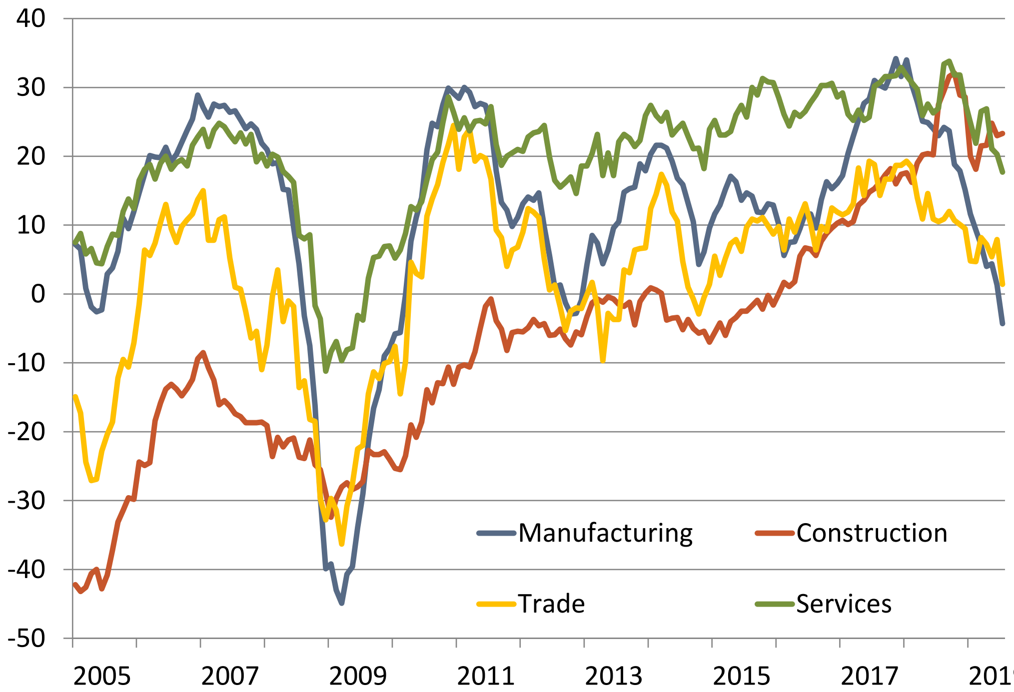
German fiscal stimulus? Do not expect much for now. Despite the economic weakness, political appetite for a major stimulus remains low in Germany. Berlin already plans a modest fiscal expansion of up to 0.3-0.4% of GDP in 2019 combining public investment and social spending. It may decide to add another boost of 0.1-0.2ppt of GDP via more generous subsidises for temporary underemployment on the job ("Kurzarbeitergeld") and cash subsidies for exchanging old cars for newer cars like in 2008/2009. Going even further than that is complicated by the different approaches that the CDU and SPD coalition partners would liked to take. In their coalition agreement of March 2018, CDU/CSU and SPD pledged to reduce the solidarity surcharge to the income tax by about €11bn in 2021. The CDU/CSU would have liked to go further and fully abolish the surcharge (about €20bn, 0.6% of GDP) in 2020 already. The more left-leaning SPD has so far vetoed that.

Chart 1: Ifo business climate, current assessment and expectations



Indexed at 2015=100. Source: Ifo

Chart 2: Ifo business climate by sector



Source: Ifo

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