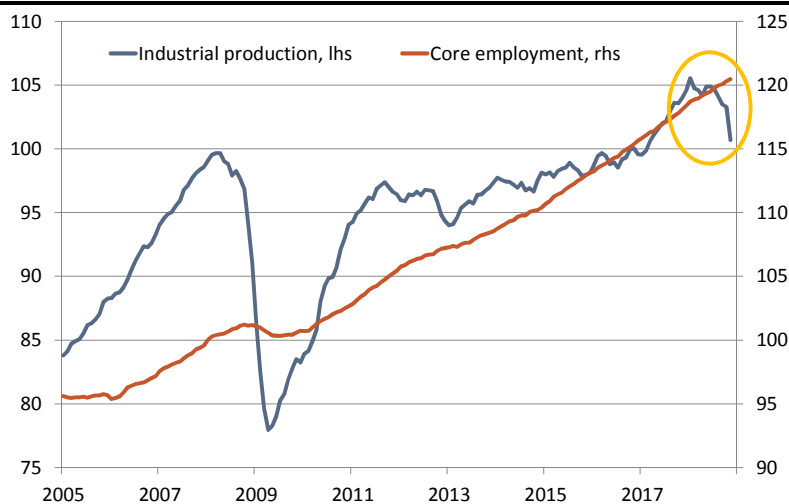


11 January 2019

## Solid growth or recession? Two sides of the German story

German core employment and industrial production (January 2008 = 100)



Index levels, three-month moving average for industrial output excluding construction, monthly data for November 2018; core employment not subject to payroll taxes, Berenberg estimate for November based on Destatis total employment data. Sources: Destatis, Bundesbank Berenberg

- Is Germany holding up well – or suffering a technical recession?** Recent data provide evidence for both stories. While retail sales and the labour market remain solid, export-oriented industry seems to be plunging. A sharp fall in November left the October/November average for industrial output 1.7% below the Q3 level. In Q3, a less pronounced 1.3% qoq drop in output caused a 0.2% qoq decline in GDP. Judging by industrial data, German GDP may have contracted again in Q4. A likely rebound in December data and the strength outside industry should still prevent that. But we certainly cannot rule out that Germany may have suffered a technical recession in late 2018.
- The trouble with cars:** In Q3, the belated adjustment to new emission testing standards caused an 8% plunge in output of cars and car parts, subtracting almost 0.4% from Germany's Q3 GDP. This problem is not over yet. Car companies cannot yet produce as many cars as they could sell as some models are still not certified under the new standards. Car sector output fell by a further 0.7% in October and November relative to the Q3 average. However, the trouble looks set to fade. Buyers are back. In November, car orders rebounded to the best level since late 2018.
- Blame the weather?** Last autumn, unusually low water levels on the Rhine disrupted the transport of chemicals. This caused a 10% drop in output of chemicals in October and November. Otherwise, German factory output in October/November would have been just 0.7%, instead of 1.7%, below the Q3 level. With normal rainfall now raising water levels again, this disruption will soon be over. Abstracting from the special car and weather factors, the data for export-dependent industry indicate near-stagnation but not recession for the German economy.
- The strength at home:** Backed by an almost undiminished pace of employment growth as well as stronger wage increases, and supported by the recent drop in oil prices, German retail sales rose strongly in November, pushing the October/November average 0.6% above the Q3 level. Anecdotal reports about a good Christmas shopping season suggest that private consumption advanced 0.6% qoq in Q4. Domestic demand remains firm.
- The labour market counts:** With its 2004 reforms, Germany turned itself into a great place to invest and create jobs. As companies want to hire ever more qualified workers, they rarely dismiss people even when demand drops off temporarily. The 2008/2009 mega-recession barely registered in the labour market (see chart). We expect employment and income growth to remain solid in the current downturn. Once sentiment brightens if and when trade tensions are defused, China stimulates its demand and the UK avoids a hard Brexit, German industry is likely to bounce back, helping the economy to return from near-stagnation now to at least trend growth later in 2019.

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