Florian Hense, Economist | florian.hense@berenberg.com | +44 20 3207 7859

GERMAN ECONOMY: SUFFERING LESS THAN OTHERS

Berenberg Macro Flash

In the realm of the blind the one-eyed man can have the edge: The German economy contracted by 2.2% qoq in Q1. According to Germany's statistical office Destatis, construction investment and public expenditures contained the damage. Private consumption and equipment investment fell significantly. Both exports and imports also contracted sharply.

While the drop is smaller than during the worst quarter of the financial crisis (Q1 2009), the most serious damage of the Covid-19 is yet to come. The economy has probably started to recover gradually as first lockdowns were eased in late April and will likely continue to do so for the remainder of Q2. However, that recovery is unfolding from the extremely depressed levels of economic activity between mid-March and mid-April. For Q2, we expect a drop by c13% qoq (see Chart 1).

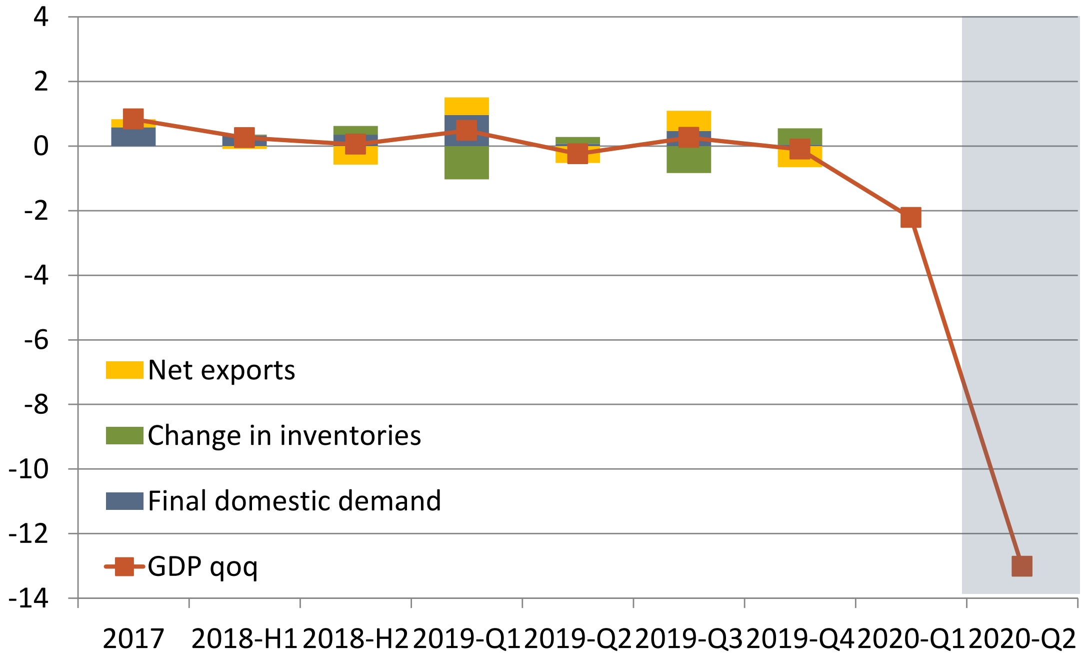
Doing less badly: Still, the German economy seems to be faring better than the other major European economies this year (we expect -7.5% for 2020 vs. the Eurozone's -9.5% and the UK's -9%) for a number of reasons:

1) Germany has been hit less badly by the pandemic in terms of confirmed cases per capita (see Chart 2) – partly due to luck, partly because it responded quickly to the spread of the pandemic. German authorities could therefore afford to impose slightly softer restrictions to daily life (see Chart 3) than other countries with economic activity less affected.
2) The fiscal response is among the biggest and most comprehensive judging by the discretionary stimulus, loan guarantees and potential tax deferrals.
3) The above-average share of its export-oriented manufacturing sector usually makes the German economy more prone to swings in the global economy (see Chart 4). During the period of the Covid-19 containment measures, however, shops and other providers of domestic services are affected even more badly than factories.
4) Germany's public services are experienced in handing out job retention payments. Its *Kurzarbeitergeld* has been tested and proven during the financial crisis 2008/09. In places elsewhere such as Italy the money is reportedly not reaching all people.

The three risks to watch:

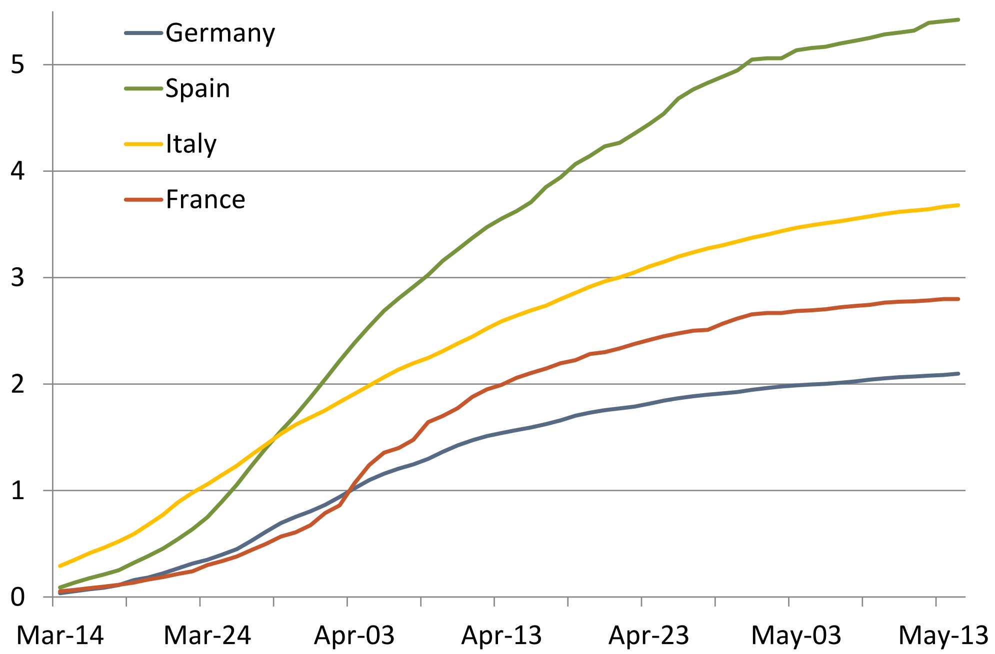
- A second major infection wave which would trigger harsh and long restrictions to be re-introduced hitting activity and confidence yet again.
- An escalation of the tensions in the Eurozone. Given its strength, Germany can afford to support those neighboring countries which have been hit harder. It is in Germany's own interest to make sure places such as Italy and Spain recover as quickly as possible from the Covid-19 recession. Otherwise Germany would struggle to fully recover, too. After all, it still relies heavily on the export of manufactured goods to its European neighbours. What is somewhat containing the damage now could turn again into a big drag going forward.
- A potential new trade war between the US and China. Hopefully, neither country will really want to impair its own recovery prospects by going down that route.

Chart 1: German GDP growth and its contributions by expenditures



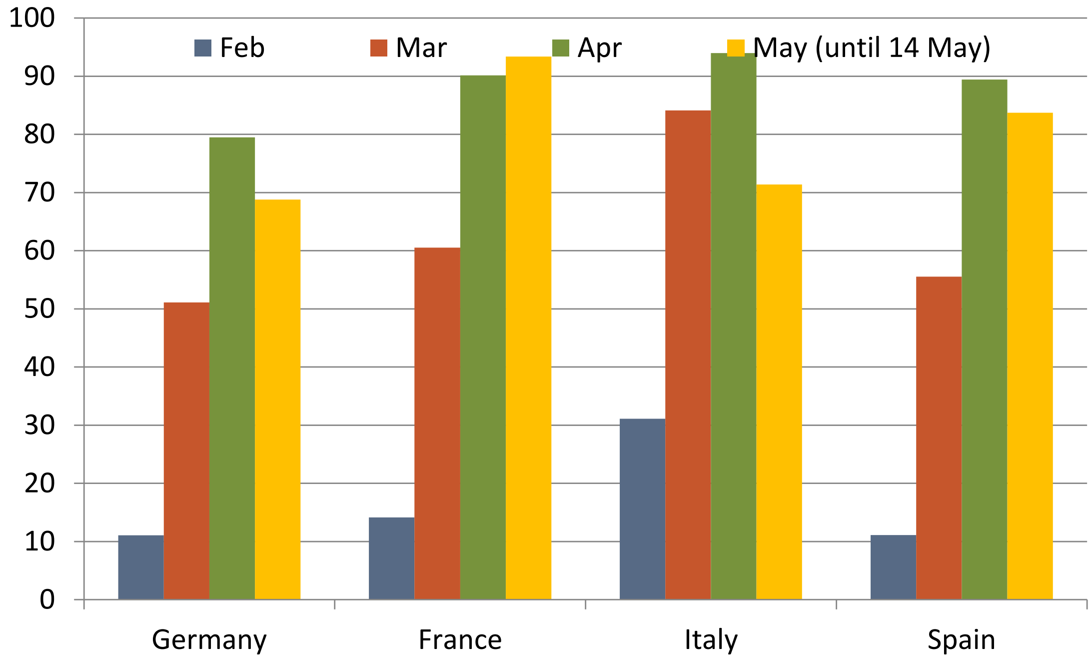
Qoq GDP growth in %, contributions in %-points. No contributions for Q1 and Q2 2020. Berenberg GDP projection for Q2 2020. Source: Destatis, Berenberg

Chart 2: Confirmed cases per 1000 capita



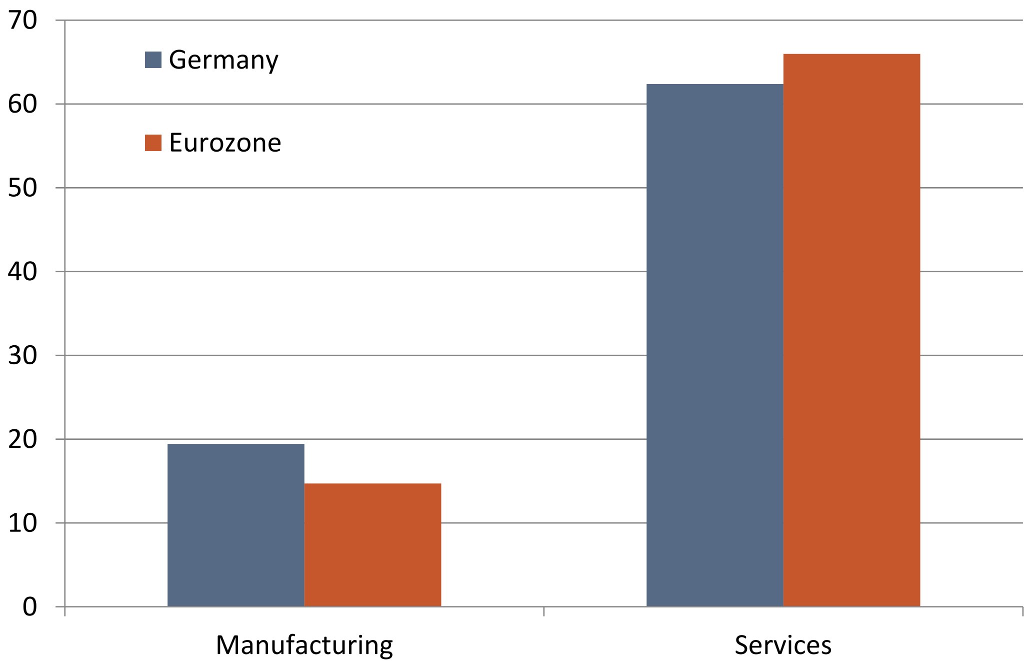
Source: Johns Hopkins University

Chart 3: Stringency of lockdown measures (0-100 – the higher the harsher/longer containment measures)



Stringency index of Oxford University from 0 (least stringent) to 100 (most stringent). Source: Oxford University, Berenberg

Chart 4: Share of manufacturing and services sector relative to GDP (in %)



Source: Eurostat, Destatis, Berenberg

Joh. Berenberg, Gossler & Co. KG
60 Threadneedle Street
London EC2R 8HP
Phone +44 20 3207 7859
www.berenberg.com
florian.hense@berenberg.com