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GERMAN ECONOMY: HISTORIC PLUNGE

Berenberg Macro Flash

Even worse than expected: In the second quarter of 2020 the German economy contracted by more than in any quarter since 1970 – the year the official German GDP series, published by Destatis, starts – and probably since World War II. Amid the Covid-19 pandemic and the measures to contain its spread, German GDP plunged by 10.1% qoq, wiping out nearly 10 years of growth. So far, the biggest contraction in a single quarter was in Q1 2009 (-4.7%). According to the Destatis press release, with the exception of some increase in government spending, all components of GDP – household consumption, equipment investment and exports – fell sharply (Note: Destatis only provides a qualitative breakdown of GDP with the first estimate). Together with the first quarter decline of 2% qoq (revised up from -2.2%), the combined 12% drop in GDP from the pre-crisis level in Q4 2019 trumps the peak-to-trough fall during the financial crisis of 7%, which happened over four quarters (from 2008 Q1 to 2009 Q1). Chart 1 shows the unprecedented size and speed of the Covid-19 recession relative to the financial crisis and other previous downturns over the past 50 years.

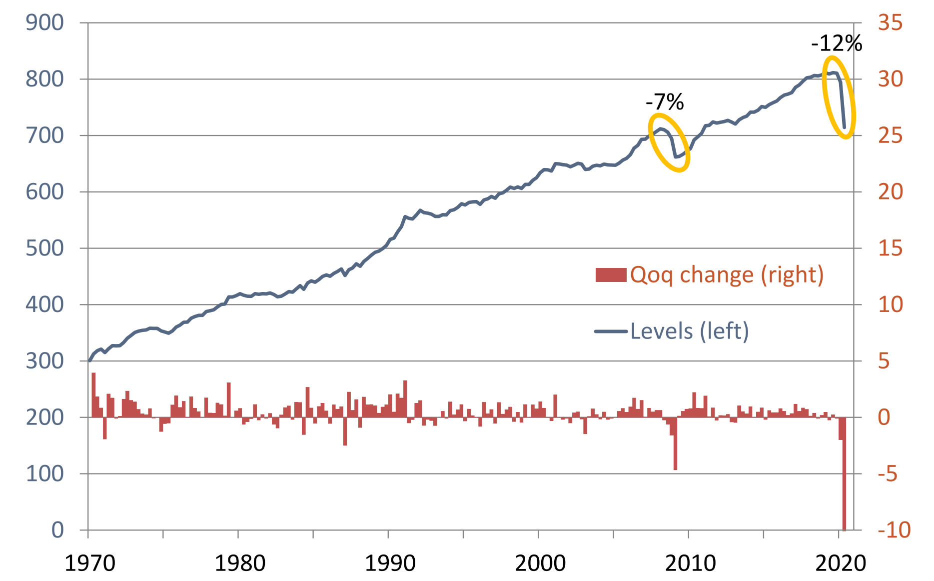
Treat the first estimate with even more caution than usual. For the first time, Destatis has published a flash estimate 30 days after the end of a quarter. Previously it did so only 45 days after. Destatis may thus have to revise its first estimate more than in the past – as it pointed out itself. Crucially, Destatis lack the hard data for June and, instead, base their estimate on projections of how the economy did. Amid significant uncertainty about current activity this challenge is even more daunting than usual. While higher-frequency data such as retail footfall data, flight statistics and truck mileage provide a guide to current trends, it remains unclear how closely some of the newly-watched measures track official statistics. We see a good chance that Destatis eventually upgrades its estimate to closer to our or consensus' slightly less negative calls (Berenberg: -8.5% and consensus -9%) going forward. The Q2 reading creates some downside risk to our 2020 full year call of -6%.

It could have been much worse: First, the quarterly GDP number camouflages the plunge in activity to probably more than 20% below pre-crisis levels in April. A rebound in activity from May onwards, which gained more momentum during June, lifted the quarterly GDP average and limited the contraction relative to Q1. Second, the German economy probably suffered less badly than Italy, Spain and many other Eurozone countries. Fortunately for Germany, softer and shorter lockdown measures sufficed to contain the pandemic. The hit to economic activity was therefore also smaller. In addition, the German government responded with one of the most comprehensive fiscal stimuli around the globe which further softened the blow to the economy and accelerated its recovery. The German Q2 performance points to a small downside risk to our Eurozone Q2 GDP call published tomorrow (Berenberg: -12%).

Outlook: Both the high-frequency data and the traditional monthly survey data (Ifo, PMIs and the just released economic sentiment survey by the European Commission) suggest activity picked up further during the first month of Q3. Helped by a base effect, Q3 should show a strong rebound in GDP relative to a Q2 depressed by a very weak April. With luck, the economy may recover some 40% of its Q2 losses in Q3. The real question is how the rebound evolves over the medium-term. The rebound was so far of mechanical nature. As lockdown measures eased, shops and restaurants opened, activity recovered naturally. This explains the initial significant but not quite V-shaped recovery over the past few months from the April trough. It is unclear how quickly and significantly the pace of recovery levels off. Once most supply is switched back on again, the pace will depend largely on how demand recovers. Second wave fears could constrain household consumption and business investment. Foreign demand will likely remain sluggish as important trading partners of German exporters, including the US take more time to bring the pandemic under control. At the same time, the fiscal/monetary policy stimulus in the pipeline is vast. The small loss in employment so far shows that the stimulus measures are helping to soften the blow. For now we stick to our view for a tick-shaped recovery along which the German economy could reach its pre-crisis GDP level in early 2022 and most of Europe in 2022.

Unemployment – unexpected rise: While the July drop in unemployment of 18k may be an outlier, to which a redirection of tourists from Mediterranean beaches to domestic destinations and some possible hiring in that sector may have contributed, today's labour market report suggests that employment could soon bottom out.

Chart 1: German GDP quarterly levels (in bn) and changes (qoq, in %)



Sources: Destatis, Berenberg.

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