

Germany Business Forecast Report Q1 2015

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Abstracts

Core Views

Our long-held bearish view towards the German economy appears to be playing out. We have moved even further below consensus on German growth for 2014/15, as weakening confidence will cap both investment and consumption growth over the coming quarters. While we believe Germany's current account surplus has peaked, narrowing of the surplus over the next five years will be limited by tight fiscal policy, which will in turn hamper the regional economic recovery.

German energy policy will continue to drive significant structural economic imbalances. While attempts to shield industry from the cost of transition towards renewable energy resources will curtail consumption, German industrial competitiveness will eventually suffer from higher energy costs.

We expect German foreign policy to become increasingly isolationist over the next few years, driven by the declining global influence of the US, changing attitudes of a younger generation and fatigue with the lack of reform among eurozone states.

Major Forecast Changes

We believe that the regional fallout from the Ukraine crisis exacerbated the recent collapse in leading and coincident indicators, hence our decision to move even further below consensus on growth for 2014 and 2015 – to 1.1% and 1.3% from 1.5% for both, taking us even further below consensus (currently at 1.5% and 1.8% according to Bloomberg surveys).

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CHAPTER 1: POLITICAL OUTLOOK

SWOT Analysis
BMI Political Risk Index
Domestic Politics
AfD Not A Flash In The Pan

The eurosceptic Alternative fur Deutschland (AfD) party is set to remain a political force in Germany in the years ahead as tepid economic growth and growing antipathy towards the EU enhances disillusionment with establishment parties. The AfD will not pose a threat to the ruling Christian Democrats directly, but could force the government to adopt a tougher line towards profligate EU member states to avoid leaking support to the AfD.

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Difficult Decisions Ahead

Although it is one of the most stable countries in the world, Germany must make some difficult political choices over the next 10 years. Some of these, such as how to deal with a rapidly ageing population, can be addressed without threatening political stability, while others, such as re-defining Germany's role in Europe, could prove more destabilising.

CHAPTER 2: ECONOMIC OUTLOOK

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BMI Economic Risk Index
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Structural Weaknesses Emerging

Eroding export competitiveness and slowing external demand will continue exposing Germany's structural economic weaknesses over the next few quarters. Lack of political will to address these problems will severely restrict Germany's long-term rate of growth.

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Fiscal Policy

Few Benefits Of Tight Fiscal Policy

Germany's 2015-2018 fiscal plans are too modest to support growth. Balanced budgets and a declining debt burden means Germany will remain a regional safe haven, but fiscal policy will not help periphery eurozone economies escape low growth/high debt dynamics, nor allow Germany to overcome its sizeable infrastructure deficit.

TABLE: Fiscal Policy

Balance Of Payments

Sluggish Rebalancing Impedes Regional Recovery

Germany's current account surplus peaked at 6.8% of GDP in 2013, but domestic demand will not be strong enough in the coming years to support eurozone rebalancing or a stronger regional recovery. By perpetuating eurozone savings imbalances, impeding a more robust recovery and encouraging investment into low yielding assets, Germany's current account surpluses offer minimal long-term benefit for the German economy.

TABLE: Balance Of Payments

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ECB Easing: Signs Of Growing Anxiety

The ECB has embarked on additional monetary easing at the September meeting, earlier than we had expected. The ECB's almost knee-jerk reaction to the longstanding deterioration in headline inflation and macro data suggests that the central bank has started to backpedal fast, having previously played down the risks of deflation. We do not view the new measures as a major new expansion of monetary policy, but believe that the ECB's actions and reference to the size of its balance sheet indicate that the tide is starting to turn, and that far more aggressive monetary stimulus could be on the cards.

Banking Sector

Growth To Improve, But Profitability Weak

The state-run pillar of Germany's banking sector will continue to dominate non-bank lending over the coming quarters at the expense of the commercial banks. Meanwhile, corporate bond issuance by non-financials will remain popular as companies seek alternative financing to traditional bank loans, which will further limit industry growth and profitability.

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The German Economy To 2023

Economy Losing Its Shine

Germany's economic prowess is set to fade over the next decade, as productivity gains

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