

Editorial



Dr Gustav A. Horn,
Head of the Department of Macro
Analysis and Forecasting, asks:

"Will the upturn continue next year?"

Germany's economy continues to recover. The stagnation that had persisted until the end of last year has been overcome, and the economy is currently expanding at an annualised rate of around 1.5%. There is, however, an unusually deep split between domestic demand and exports. Almost all the expansion derives from export growth, whereas domestic demand has remained stagnant. Consumption, in particular, is still very weak, and the crisis in the construction sector is far from over. Against this backdrop, the German economy can be expected to grow by about 1.8% this year.

The more interesting question is whether this growth will continue next year, and opinions differ in this regard. Most forecasters expect a slowdown. They fear that German exports will lose steam because the global economy will grow less robustly than this year. The U.S. and the Chinese economies, especially, they believe, will exhibit much weaker growth. They further assume that structural problems will prevent the German economy from growing any faster and therefore estimate potential growth at between 1% and 1.5%. If this assessment is correct, it is reasonable to estimate 1.8% as a peak in the business cycle.

These forecasts seem negatively biased. Firstly, there will be only a minor global economic downturn. In particular, growth in the euro zone can even be expected to accelerate. This is very important for the German export economy, given that Europe is its main market. Moreover, wage rises in Germany have been very moderate by international standards. This has led to much lower inflation rates in Germany than in the rest of the euro zone. Consequently, the competitiveness of firms producing in Germany has improved significantly in recent years. This is why German exports are so strong. And this strength will actually intensify next year, so that even when faced with a slightly cooler world economy, German exports can be expected to remain robust, which will in turn benefit the domestic economy. Moreover, a vibrant export economy will also strengthen investment, so that domestic demand will probably also emerge from stagnation next year. But there is still one piece of bad news. Private consumption will remain weak as a consequence of the moderate wage increases, and this will prevent the German economy from entering a boom phase. It is not structural problems that are a major dampener for growth in Germany, but rather a yawning lack of domestic demand.