

Joint Economic Forecast Spring 2015

Press release

Embargo: Thursday, 16.04.2015, 11.00 a.m.

16 April 2015

Joint Economic Forecast Spring 2015: A Strong Upswing Thanks to Cheap Oil and a Weak Euro

The German economy is experiencing a strong upturn driven by unexpected expansive impulses, especially the falling oil price and the sharp depreciation of the euro. Gross domestic product is expected to increase by 2.1 percent this year. The 68 percent projection interval ranges from 1.1 percent to 2.8 percent. Consumption is the driving force behind the upturn. The rest of the euro area is also expected to produce slightly positive impulses, meaning that international trade will contribute to growth. The pace of growth is only expected to slow slightly in the year ahead. The euro's depreciation will continue to stimulate the economy, while the positive effects of the lower oil price are expected to fade. Public budgets will show significant surpluses of over twenty billion euros in 2015 and 2016 respectively. In view of large structural surpluses, the time is ripe to make the income tax rate more performance-oriented – especially for small and medium-sized companies.

World production is expected to expand at a slightly faster pace in spring 2015. Strong impulses will come from the sharp drop in the crude oil price, which has almost halved since June 2014. The oil price drop is mainly due to oil-market specific causes and contributed to an economic upturn in advanced economies back at the end of 2014. In the major emerging economies, by contrast, the economic climate remains fairly weak overall. China's growth rate has been declining since mid-2014 as a result of falling real-estate prices. In Brazil production is overall stagnating, and Russia is currently in a recession.

On the whole, monetary policy has become even more expansive in recent months, while the gap between the monetary policies pursued by the major advanced economies has widened. The Bank of Japan extended its existing bond buying programme back in October and the ECB launched an extended programme in March. However, the central banks in several emerging economies have lowered their interest rates in recent months. The US Federal Bank, by contrast, is continuing to gradually tighten its monetary policy. It wound down its bond purchasing programme at the end of 2014. The Fed is expected to increase the Federal Funds Rate in 2015. The growing divergence in monetary policy orientation has meant that several currencies, including the euro and the yen, have depreciated significantly against the US dollar since last summer. Monetary policy worldwide is expected to remain markedly expansive during the forecasting period. US interest rates will only be raised in small steps, while the ECB will continue to implement its policy of quantitative easing until at least September 2016.

Fiscal policy is expected to remain marginally restrictive in advanced economies in 2015 and 2016. In the USA and the euro area the fiscal policy stance measured by the structural budget deficit is more or less neutral. Although fiscal policy will remain restrictive in Japan in 2015, the contractive effects generated by it are expected to be smaller than last year. Many advanced economies have recently relaxed their fiscal policy stance as a result, because the interest burden on public budgets has fallen.

The world economy is expected to continue to pick up over the course of this year. The oil price will support the economy as a whole, as it will lead to a redistribution of income from oil-producing to oil-importing economies. In the latter a large share of national income will be spent on consumption or investment. In addition, the export business in euro area countries and in Japan will be stimulated by the drop in the exchange rate against the US dollar. Overall, the economy, especially in advanced economies, is expected to gain impetus this year.

Production in emerging countries will be stimulated by the economic upturn in advanced countries. Oil-importing countries stand to benefit from the sharp decrease in oil prices. However, this is not expected to lead to a strong upturn in economic activity in emerging countries. Countries with high commodity exports, especially in Latin America, have suffered from the downturn in commodity prices. Domestic economic problems are also widespread. The Chinese economy, for instance, is currently suffering from a drop in real-estate prices.

Dampening effects are expected to gain impetus in advanced economies later on in the forecasting period. Monetary policy in the USA and in Great Britain will be less expansive, which will have a dampening effect on the domestic economies of both countries and is expected to trigger an increase in capital market interest rates in other countries due to the international interest system. The emerging economies will also be affected by this development. In short, the institutes expect a 2.9 percent increase in world production this year and a 3.2 percent increase in the year ahead.

There are a series of risks to world economic development over the forecasting period. The impact of the interest rate turnaround in the USA on asset prices in industrialised countries, as well as on capital flows in key emerging economies remains uncertain. The economic situation in China also presents risks. The significant downturn in real-estate prices in China is placing a heavy burden on the financial sector, especially given that Chinese companies and regional authorities have high debts. Conflicts between Russia and the Ukraine and in the Arab world could escalate at any time. In this scenario oil prices could rise fast, or uncertainty could grow in the financial markets. Greece's renewed financial problems also pose a serious threat to Europe's economy.

The German economy is experiencing a sharp upturn. It is being stimulated by unexpected, expansive impulses, especially by the drop in oil prices and the strong depreciation of the euro. Gross domestic product is expected to have increased by 0.6 percent in the first quarter. The upturn looks set to lose impetus somewhat over the course of the year, but capacity utilisation rates will continue to rise. Thanks to the strong start to the year, among other factors, the institutes expect gross domestic product to increase by 2.1 percent in 2015, with 0.2 percentage points due to a higher number of working days. The institutes expect overall economic production to increase by 1.8 percent in 2016.

Private consumption is fuelling the upturn. It is benefitting from the drop in oil prices, which is boosting consumer purchasing power. Rising wages due to the favourable labour market situation are also stimulating private consumption, which is expected to increase by 2.5 percent this year and by 1.6 percent in 2016.

Exports will be boosted into next year by a significant increase in price competitiveness. The institutes estimate that its contribution alone to the increase in exports will amount to 1.0 percentage points this year and around 0.5 percentage points in 2016. The uptick in the euro area's economy will also have a slightly positive impact on exports. In addition, however, imports are expected to rise sharply thanks to robust domestic demand, meaning that international trade is only expected to make a small contribution of 0.3 percentage points to the increase in gross domestic product in both years on balance. The current account surplus in relation to gross domestic product will rise to 8.5 percent, primarily due to significantly lower import prices.

Levels of corporate investment are gradually expected to rise. In view of strong demand from private households, consumer-related industries and service branches in particular will steadily increase their capacity utilisation. Rising exports in the euro area will also provide fresh impulses. All of these factors are expected to boost investment in equipment over the course of the year, especially if corporate profits increase due to falling oil prices and financing conditions remain favourable. A number of constraining factors are nevertheless expected to impact the economy. The pace of growth in many large emerging economies will remain measured and the future of the currency union remains uncertain. Several national economic policy decisions like the introduction of a minimum wage are ultimately expected to continue to hamper companies' willingness to make domestic investments. Residential construction continues to follow an upwards trend boosted by favourable developments in income and low returns on other types of investment.

The employment outlook remains very favourable. The introduction of the legal national minimum wage, however, is leading to declines in minimal employment. Based on current data, minimal employment is expected to drop by 220,000 persons over the forecasting period. Marked growth in production, by contrast, is expected to lead to a strong employment dynamic in jobs liable to social security contributions, and the number of persons in employment is expected to rise by around 350,000 this year, and by just under 250,000 in 2016. Against this background, the unemployment rate will continue to drop to 6.3 percent this year and 5.9 percent in 2016.

The institutes forecast a slight upturn in inflation. They no longer expect oil prices to have any dampening effect on prices. The increase in the costs of imported goods and services due to the significant depreciation of the euro will increasingly be passed on to consumers over the forecasting period. In addition, rising capacity utilisation will also increase scope for passing on higher costs in the production process. Inflation, however, which is forecast at 0.5 percent this year and 1.3 percent in 2016, will remain clearly below the 2 percent mark.

Public budgets will probably post significant surpluses of over twenty billion euros in 2015 and 2016 respectively. With the output gap almost closed, the structural surplus, adjusted for economic influences, will be around the same amount. The resulting financial leeway should be used to initiate a reform of Germany's taxation and contributions system. Thanks to the relatively high burden of the labour factor in Germany by international comparison, the institutes see an urgent need to take action. The tax wedge between labour costs and net wages, created by contributions to the pay-as-you-go social security system and income tax, is among the highest of all OECD countries in Germany. The income tax rate above all – especially for small and medium-sized companies – should therefore be made more performance-oriented to reduce the labour factor burden and thus to increase Germany's growth potential.

Since the drop in crude oil prices has a major influence on the development of the economy as a whole in Germany, this report features an entire section on that topic. The fall in oil prices seen since summer 2014 has probably reflected both oil market-specific factors and developments in the world economy. Thanks to the changed offering structure in the oil market, especially the growing market share of unconventional crude oil, there are several indicators that the crude oil price is set to remain low for some time. This will have opposing effects on the German economy. Although demand for German goods is expected to drop due to the falling revenues of oil-exporting countries, German households will benefit from higher real income levels and the German economy, like other net crude oil importers, will enjoy an improvement in terms of trade. Overall, the positive effects will prevail. Should the oil price rise once again, contrary to the assumptions made in this forecast, this would have a dampening effect on the German economy.

Key Forecast Figures for Germany

	2011	2012	2013	2014	2015	2016
Price adjusted GDP (percentage change over previous year)	3.6	0.4	0.1	1.6	2.1	1.8
Persons in employment ¹ (1 000 persons)	41 570	42 033	42 281	42 652	43 007	43 242
Unemployment (1 000 persons)	2 976	2 897	2 950	2 898	2 723	2 568
Unemployment rate ² (in %)	7.1	6.8	6.9	6.7	6.3	5.9
Consumer prices ³ (percentage change over previous year)	2.1	2.0	1.5	0.9	0.5	1.3
Unit labour costs ⁴ (percentage change over previous year)	0.4	3.1	2.2	1.6	1.9	1.7
General government financial balance ⁵						
EUR billion	-23.3	2.6	4.2	18.0	20.7	25.6
in % of GDP	-0.9	0.1	0.1	0.6	0.7	0.8
Balance on current account						
EUR billion	164.6	187.3	182.0	219.7	256.0	266.0
in % of GDP	6.1	6.8	6.5	7.6	8.5	8.5

1 Domestic employment.

2 Federal Employment Agency concept, unemployed persons as % of civilian labor force.

3 Consumer price index (2010 = 100).

4 Compensation of employees per hour worked by employees in relation to labour productivity (per hour worked by persons in employment).

5 On national accounts definition (ESA 2010).

Source: Federal Statistical Office, Federal Employment Agency, Deutsche Bundesbank, 2015 and 2016: forecast by the Institutes.

Members of the Joint Economic Forecast Project Group:

Deutsches Institut für Wirtschaftsforschung e.V.
www.diw.de
Press contact Tel.: (030) 89789 252, Email: presse@diw.de
in cooperation with:
Österreichisches Institut für Wirtschaftsforschung
www.wifo.ac.at

Leibniz-Institut für Wirtschaftsforschung Halle
www.iwh-halle.de
Press contact Tel.: (0345) 7753 720, Email: presse@iwh-halle.de
in cooperation with:
Kiel Economics
www.kieleconomics.de

ifo Institut – Leibniz-Institut für Wirtschaftsforschung an der Universität München e.V.
www.ifo.de
Press contact Tel.: (089) 9224 1218, Email: schultz@ifo.de
in cooperation with:
KOF Konjunkturforschungsstelle der ETH Zürich
www.kof.ethz.ch

Rheinisch-Westfälisches Institut für Wirtschaftsforschung
www.rwi-essen.de
Press contact Tel.: (0201) 81 49 244, Email: katharina.brach@rwi-essen.de
in cooperation with:
Institut für Höhere Studien Wien
www.ihs.ac.at