2.2. GERMANY

Germany’s real GDP growth rebounded tangibly from a near-recession in late 2018 to 0.4% in the first quarter of 2019. The normalisation of automotive sales had an appreciable effect across the board in exports, investment, private consumption and inventories. Private consumption growth was also stimulated by fiscal measures which had a positive impact on retail sales and consumer services. Export growth was broad-based geographically and was partly boosted by frontloading of deliveries to the UK in anticipation of Brexit. While import growth was solid, overall net exports contributed positively to GDP growth.

Construction investment increased further, reflecting strong housing demand and infrastructure needs and the benefit of favourable weather conditions. Although capacity utilisation levels decreased, equipment investment growth strengthened in a number of asset types including not only vehicles but also electronics and machinery.

Prospects for the rest of the year, however, look less bright and the forecast for quarterly real GDP growth has been revised down compared to spring. In particular, the second quarter seems to have seen a decline in economic activity. Part of this reflects a statistical ‘payback’ for the strength of growth in the first quarter while the cooling of overall economic sentiment has deepened in recent months. Survey data point to a deterioration in foreign demand and a weakness in order inflows and industrial activity. The automotive sector in particular will likely continue to grapple with the deterioration in the external environment, as well as lingering uncertainty about trade policy and consumer preferences. German exporters are also concerned that any escalation in protectionism would likely weigh on business confidence across the globe and thus dampen global investment demand.

On the other hand, domestic demand is proving resilient and should support a recovery in the second half of the year. With unemployment at a record low and solid wage growth, private consumption should continue to sustain growth. Public consumption growth is expected to resume later in the year.

Overall, real GDP is now forecast to increase by 0.5% in 2019 and by 1.4% 2020, slightly less than expected in the spring. The stronger-than-anticipated outcome in the first quarter explains the unchanged annual figure for this year, despite the downward revisions for the rest of the year. Economic activity will receive an additional boost of almost 0.4% in 2020, thanks to a significant working day effect. Risks are tilted to the downside and stem mainly from the deteriorating external environment, but also domestic, as the negative sentiment in the manufacturing sector could spill over to the currently resilient services sector, as well as to consumer confidence.

Core inflation (excluding energy and unprocessed food) is expected to stay unchanged in 2019 and marginally increase in 2020, driven by solid wage growth and consumer demand. Inflationary pressures do not seem as acute, as in some of the consumer services sectors the pass-through is muffled by productivity increases. Energy prices are projected to decrease and are expected to exert a disinflationary effect. Overall HICP inflation is expected to ease from close to 2% in 2018 to 1.4% in 2019 and 1.3% in 2020.