# GERMANY



## GROWTH HAS WEAKENED, BUT EMPLOYMENT IS RESILIENT

**Germany is the Western European country where GDP growth was the most negative in Q4 2022 (-0.4% q/q). Furthermore, economic indicators, although improving, remained relatively weak at the beginning of 2023. A further contraction in GDP in Q1 2023 therefore remains our central scenario. However, more favourable signals (slight disinflation, reopening of China, reduced supply shortages in the automotive sector) could lead to a return to growth from Q2. This has already been reflected in household confidence, although the weakness of growth in the euro area, since Q4 2022, could limit the intensity of this recovery.**

Germany recorded a drop in its GDP in Q4 2022 (-0.4% q/q), in line with economic surveys. This was not the case in Q3, where GDP growth was positive despite deteriorated surveys (business climate, household confidence): a favourable figure which therefore led to a subsequent setback.

After three quarters of continuous growth (despite a deterioration in household confidence), private consumption fell in Q4 (-1% q/q), as a marked acceleration in inflation weighed on it (up to 11.6% y/y in October 2022). Investment in machinery and equipment also fell (-3.6% q/q), after a very good figure in Q3 (+5.4% q/q). Measured year-on-year (y/y), however, this investment continued to grow by 4.5% in Q4. A more structural reduction seems to apply to investment in construction (-2.9% q/q in Q4 and -6.8% compared to Q1 2022), which seems affected by the rise in interest rates.

### SUPPLY CONSTRAINTS STILL PREDOMINANT

The proportion of companies reporting in the European Commission's Business Climate Survey that demand pressures are limiting their production has increased: 16% of manufacturing companies in Q1 2023 (compared to 11% a year ago), highlighting the weakening of the German economy. However, labour shortages are limiting production for an unchanged proportion of companies in industry (29%, the same as a year ago) and for an increased proportion in services (30% compared to 26% a year ago). These tensions are continuing to fuel significant job creation (457,000 in 2022, of which 112,000 in Q4), keeping the labour market under pressure and at the same time supporting household income. This good momentum continued in January (64,000 jobs created).

Supply difficulties are still limiting production for 47% of the companies surveyed, compared with 76% a year ago. The partial removal of these obstacles allowed German companies to replenish their inventories: the balance of opinion corresponding to their inventories of finished products reached 7.9 points in industry in February (European Commission survey) compared to -13.8 a year previously, and 7.5 as an historical average. The positive contribution of changes in inventories in Q4 2022 (0.4 points) therefore limited the negative impact of the contraction in demand on growth.

### WHAT IF THE GERMAN RECOVERY CAME FROM... GERMANY?

In the past, for example in 2010, the growth recovery was largely driven by exports. Will the situation be different this time?

Admittedly, Germany has dual characteristics: in the S&P Business Outlook survey, it saw the sharpest improvement worldwide between October 2022 and February 2023 (by nearly 25 points), but it still has one of the most downgraded levels (only France has lower prospects). Two factors, to which Germany is highly exposed, explain the improvement: the automotive sector (fewer supply difficulties) and China (reopening of the economy with the end of the zero-Covid strategy). These support factors for the German economy nevertheless remain moderate: new car registrations are up 14% y/y over the last three months to the end of February 2023 but remain 9% lower compared to pre-Covid.

GROWTH & INFLATION

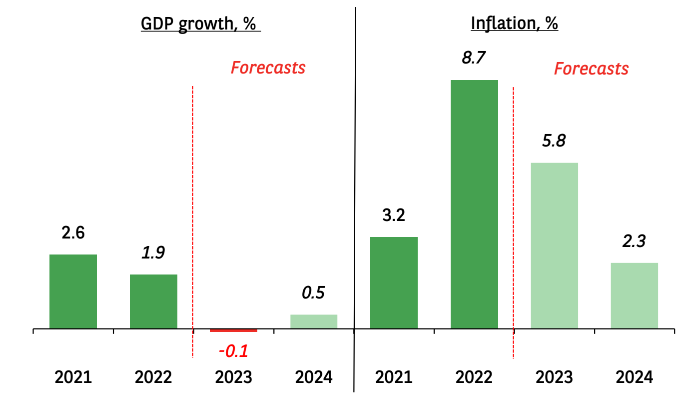


CHART 1 SOURCE: BNP PARIBAS GLOBAL MARKETS

However, more negative factors, such as the economic situation in the euro area, could hinder this recovery. As a result, the expected growth from Q2 to Q4 should not erase the negative growth carry-over effect at the end of Q1, for an annual growth forecast of -0.1%.

Above all, in our view, higher growth remains conceivable, driven by household consumption: it's a paradox because this demand item has, at no time, returned to its pre-Covid level, and its proportion in German GDP has structurally decreased compared to the beginning of the 2000s, by almost 5 points, more than any other demand item. However, disinflation which began after the peak in October 2022 (11.6% y/y) and the less deteriorated situation than expected (absence of energy supply shortages this winter) led to a rebound in household confidence, which is more pronounced for the time being in its expectations component. However, this is a characteristic of an economic recovery situation[1]. Such a recovery could be based on a more favourable purchasing power dynamic, with lower inflation, while income would be supported by a still tight labour market, as well as by the redistribution of high profits to employees.

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1See Stéphane Colliac, 'Germany vs. France: German consumers have confidence in the recovery; the French, not yet' Chart of the week, BNP Paribas, 15 March 2023.