# GERMANY



## HAS GROWTH BOTTOMED OUT?

**The German economy has been significantly underperforming the eurozone average and past standards for just over 6 years. The country might even be in recession again in Q4 2023 and Q1 2024. So has Germany bottomed out? From an economic point of view, this is likely because the moment of weakness, posted this winter, is partly due to exceptional effects. From a structural point of view, the German economy is expected to continue to post moderate growth, which would not allow it to regain its status as a driver of European growth.**

Recent data give little cause for optimism. German GDP contracted by 0.3% q/q in Q4 2023 and by 0.1% on average over 2023 as a whole. The beginning of 2024 has shown no signs of recovery. Although manufacturing production grew by 1% m/m in January, it remained 1.5% below the level seen last November. The automotive industry is a factor, with production in January almost 10% below its November level. The removal of government support for the purchase of electric vehicles had an impact from December onwards, and supply difficulties due to the Red Sea crisis affected the sector from January onwards (including plant closures).

As a result, the IFO Business Climate Index (IFO-BCI) and the Consumer Confidence Index (CCI) experienced a moment of weakness in January and February 2024, reaching levels below those seen at the end of 2023: 86.9 on average for the IFO-BCI compared to 88.5 in December; -29.2 on average for the CCI compared to -25.4 in December. All of these elements suggest negative growth again in Q1 2024 (-0.1% q/q according to our forecasts), and therefore a recession in Germany.

### AN ECONOMIC UPTURN IS LIKELY AS FROM Q2

Nevertheless, the German economy may well have bottomed out in Q1 2024. The interlude in January-February seems to have come to an end in March. The IFO-BCI (88.1) and consumer confidence index (-27.4) are close to levels seen in December 2023. This improvement should also be evident in production, in particular the automotive industry, which is expected to recover after the supply difficulties in Q1.

The rebound in growth expected in Q2 (+0.1% q/q) can be explained therefore, for the time being, by the end of a moment of economic weakness rather than by a long-term improvement in fundamentals. The combination of supply and demand constraints continues to characterise the German economy. New orders to industry, which have shown no signs of recovery in recent months, attest to low demand.

However, Germany should benefit from tail winds in 2024: a first interest rate cut by the ECB expected for June and an uptick in growth in the rest of the eurozone. However, German growth should remain lower than growth in the eurozone in 2024 (0% compared to 0.7%) and in 2025 (1.4% compared to 1.7%).

### A TRANSITION PERIOD THAT SHOULD LAST

The underperformance of German growth is nothing new. Between Q4 2017 and Q4 2023, German GDP grew by 1.2% compared to 5.5% for the eurozone. This contrasts with the previous period (Q4 2009-Q4 2017), when the situation was the opposite: +19.6% for Germany compared to +11.8% for the eurozone. Previously, the country had already experienced a period of low growth, following reunification, until 2005 (a time when Germany was described as the sick man of Europe), before its growth caught up with eurozone growth (between 2005 and 2009).

The 1990s had started with a costly transition period, as the cost of reunification had to be absorbed. Concerns about Germany's status as a production site also arose (standort deutschland debate). In addition, from a public finances perspective, German public debt and the public deficit were close to those of France.

GROWTH & INFLATION

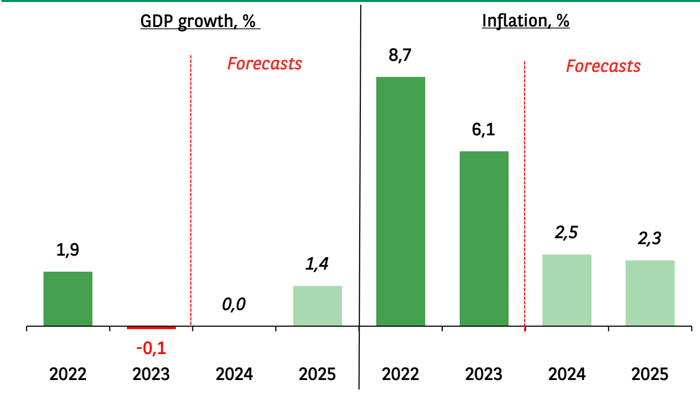


CHART 1 SOURCE: BNP PARIBAS GLOBAL MARKETS

Structural reforms ultimately closed this period on the up: the Hartz reforms (2003-05) transformed the German labour market, while public finances were governed by the debt brake rule, voted on in 2009, which limits the structural budget deficit to 0.35% of GDP. Germany also benefited from the integration of Central and Eastern European countries into the European Union in 2003 to outsource part of its production, while its exports benefited from the development of China (a member of the WTO since 2001).

Germany is now once again embarking on a transition that has two facets: adapting to climate change and taking into account the step-up in industrial policy in China and the USA. It is no coincidence that 2018 was the first year in which German growth fell below growth in the eurozone: automotive production peaked in 2017, just before the adoption of the first European standards more stringent for manufacturers (WLTP testing standards entered into force in September 2018). China's rapid industrialisation is another challenge: the country's density of industrial robots rose in 2017 from a ratio of 1 to 3 with regard to Germany to almost parity in 2022, according to the International Federation of Robotics. This step-up in the strength of China has already started to affect Germany's market share in global trade (6.6% in 2022 compared to 7.8% in 2019 according to the WTO), a decline that could become more significant.

Both transitions mean that Germany's competitive advantage is being challenged. The relative output loss is expected to continue as these transitions continue to take effect.

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