GERMANY: THE GREAT FISCAL REVERSAL

While the government has already put in place a series of measures[1] totalling EUR 65 bn euros (equivalent to 1.8% of GDP), on 29 September Olaf Scholz announced "a double whammy", to use his own words, with the introduction of measures to help with the cost of energy, up to a maximum amount of 200 billion euros. It is not expected that the entire budget will be used up; initial estimates suggest that half of the maximum budget would be utilised. This large-scale plan (5.5% of GDP) should make it possible to subsidise electricity consumption for households and businesses (around 80% of their usual consumption) and to maintain a reduced VAT rate of 7% on gas until spring 2024. After two decades of fiscal restraint, Germany is entering a new fiscal era at a time when its most precious asset, industry, is in the midst of a crisis.

As Finance Minister Christian Lindner has stated that he does not want to abandon the "debt brake", the funds disbursed will take the form of loans issued from an off-budget fund. This accounting book-entry technique is a common practice of the government, which used the same process for the climate fund and more recently for military investment. But the size of the deficits in these special funds is starting to cause concern: these are forecast to be more than EUR 50 bn in 2024 according to the Federal Ministry of Finance (EUR 27 bn for the climate fund; EUR 24 bn euros for the military fund).

At the same time, the economic situation continues to deteriorate. Industrial production fell by 2% between January and August and the decline was particularly marked for energy-intensive industries: -9.3% for the chemical and pharmaceutical industry, -7.5% in the wood/paper sector, -3.1% for steel and metalworking. Surveys of purchasing managers confirm this contraction, as the production capacity utilisation rate has fallen by 16 points since the start of 2022. The manufacturing PMI also continued to deteriorate in September and was in negative territory (-1.3 points to 47.8) for the third consecutive month. The loss of momentum in industry weighed on exports and the trade surplus, which fell to only 1.2 billion euros in August (compared with EUR 3.4 bn in July). The Kiel Institute is even predicting that the trade balance will turn negative in October for the first time since 1991. The business climate in other sectors seems to have deteriorated just as much. Worse still, the 6-monthly activity forecasts as measured by the IFO are at their lowest levels in all sectors since the 1st lockdown in April 2020. For the first time since the Covid crisis, the IFO clock reflecting where we are in the economic cycle is indicating that Germany has gone into recession.

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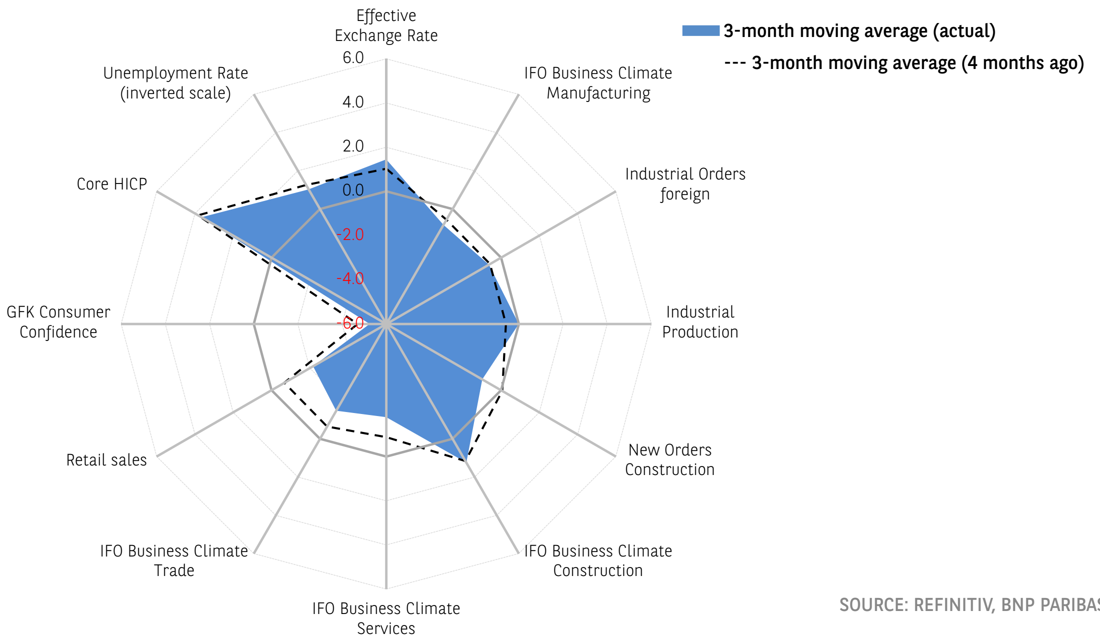
1. See EcoWeek of 19 September for details

GERMANY: QUARTERLY CHANGES



SOURCE: REFINITIV, BNP PARIBAS

The indicators in the radar are all transformed into 'z-scores' (deviations from the long-term average, as standard deviations). These z-scores have mean zero and their values are between -6 and +6. In the radar chart, the blue area shows the actual conditions of economic activity. It is compared with the situation four months earlier (dotted-line). An expansion of the blue area compared to the dotted area signals an increase in the variable.