IWH Halle Institute for Economic Research
Member of the Leibniz Association

Press Release 10/2016

KIEL ECONOMICS
RESEARCH & FORECASTING

Halle (Saale), 16th March 2016

German Economy Stays Stable Despite Shaky Environment

The German economy had a good start into the year 2016, in spite of heightened risks for the world economy and political turmoil in Europe. Employment and incomes are expanding, as is internal demand, additionally supported by government spending related to the high number of newly arrived refugees. However, sliding sentiment indicates a temporary slow down of the economy during this spring. We assume that the present political tensions inside the European Union can be mitigated in the coming months and that confidence will rise again. All in all, gross domestic product (GDP) is forecast to rise by 1.5% in 2016.

Table
Forecast for Germany: Key Economic Indicators 2015-17

	2015	2016	2017
	Percentage change over previous year (price adjusted)		
Private consumption	1,9	2,0	1,6
Public consumption	2,4	3,1	2,1
Gross fixed capital formation	2,2	2,4	2,4
Machinery and equipment	4,8	2,0	3,2
Construction	0,3	2,7	1,8
Other	2,7	2,5	2,4
Inventory accumulation[a]	−0,5	0,0	0,0
Domestic demand	1,6	2,4	1,8
Foreign balance[a]	0,2	−0,7	−0,3
Exports	5,4	1,9	4,0
Imports	5,8	4,2	5,6
Gross domestic product	1,7	1,5	1,4
For information: World production	2,5	3,3	3,6
United States	2,4	2,1	2,3
Euro area	1,5	1,4	1,5
	Percentage change over previous year		
Hours worked	1,1	0,9	0,9
Hourly union wages	2,3	2,4	2,4
Hourly actual wages	2,4	2,8	2,6
Unit labour costs[b]	1,7	2,2	2,1
Consumer price index	0,3	0,4	1,2
	1 000 persons		
Employment (domestic)	43 032	43 513	43 882
Unemployment[c]	2 795	2848	3050
	in %		
Unemployment rate[d]	6,1	6,1	6,5
Unemployment rate BA[e]	6,4	6,5	6,8
	in % of nominal GDP		
General government overall balance	0,6	0,3	0,1
Current account balance	8,2	8,0	7,8

[a] Contribution to GDP growth in % (Lundberg component). – [b] Per hour (IWH calculations). – [c] Federal Employment Agency (BA) concept. – [d] Unemployment in % of labour force (domestic). – [e] Unemployment in % of civilian labour force (Federal Employment Agency (BA) concept).

Source: Federal Statistical Office; Eurostat; Bureau of Economic Analysis; 2016 and 2017: forecast (as of March 16, 2016).

Press contact
Stefanie Müller
Tel +49 345 7753 720
presse@iwh-halle.de

Scientific contact
Oliver Holtemöller
Tel +49 345 7753 800
ohr@iwh-halle.de

Keywords
Germany, Business Cycle, Forecast, Labour Market, Production

Halle Institute for Economic Research (IWH) – Member of the Leibniz Association
Tel +49 345 7753 60
Fax +49 345 7753 820

Kleine Maerkerstrasse 8
D-06108 Halle (Saale)
Germany

P.O. Box 11 03 61
D-06017 Halle (Saale)
Germany

www.iwh-halle.de

The world economy has turned to the worse during winter 2015/2016. Production expanded at a slower rate at the end of last year, and in January and up to mid-February, worldwide oil and stock prices fell markedly. Since then, prices have recovered, but not completely. At present, markets apparently see sliding oil prices less as good news for firms and households consuming oil; instead, for financial markets, low oil prices signal weakening production activity and a higher risk that many firms or even some economies dependent on income from oil sales will go bankrupt. The size of such insolvencies, according to this forecast, will, however, be rather limited, and as most advanced economies benefit from low commodity prices, the world economy will, in spite of the ongoing slow down in emerging markets, grow at about the same pace as last year.

However, as Oliver Holtemöller, Vice President of the IWH and head of its macro-economic department puts it, "worldwide and political risks are substantial". From his point of view, the combination of the economic slow down in China, the turmoil on financial markets, risks in the European banking sector, decreasing prices in the euro area, and of the European discord on handling the large flow of refugees, might entail a genuine crisis. In particular, shrinking demand of some important Chinese industries might affect the Chinese economy as a whole and the world economy in general. Long-run risks come from interest rates staying very low for a long time and from weak price dynamics in important advanced economies. Low interest rates jeopardize, for example, the viability of life insurance schemes that contain promises of a minimal pay-out. In addition, banks' profit margins derived from term transformations might vanish if interest rates for all maturities tend to zero. Finally, the economies in the European Union bear the risk of rising political discord: For quite a few years, the case for political disintegration has gained support in many member countries. If this year in June, the British might vote for leaving the Union, the external value of the pound would go down significantly, as would investment in the United Kingdom and perhaps in other member states of the Union as well.

Weak external demand slowed the German economy down in the second half of 2015. Exports to China, for example, contracted. Internal demand, however, kept on expanding healthily. Fixed capital formation was, after an anemic summer, particularly strong at the end of the year, with strong contributions from housing and public investment. Total demand appears to have increased a bit stronger at the beginning of 2016: Industrial production jumped upwards in January, and employment continued to expand strongly. Orders for manufacturing firms, however, have increased by little, and in January and February, firms were more skeptical concerning the future than they were in the final quarter of 2015. Thus, the economy is likely to have a soft patch in the second quarter. For the second half of 2016, we expect demand to regain momentum, because many conditions continue to be quite favorable: Interest rates are very low, the external value of the Euro is – in spite of its recent limited revaluation – quite low as well, supporting the competitiveness of German producers, and both employment and incomes are rising markedly. Additional demand is caused by the high number of refugees, because public transfers are paid, dwellings are built or renovated, and administrative staff is being expanded, while taxes covering these public expenditures will not be raised. This might increase real GDP by about a quarter of a percentage point. Overall, according to this forecast, GDP growth will be at 1.5% in 2016. The consumer price level will, due to the renewed oil price fall and in general very low import price inflation, again be almost constant. Unemployment increases a bit, since a rising number of refugees will get the right to look for work but their integration into the labour market will take considerable time.

Scientific contact
Professor Dr Oliver Holtemöller
Tel +49 345 7753 800
Oliver.Holtemoeller@iwh-halle.de

Press contact
Stefanie Müller
Tel +49 345 7753 720
presse@iwh-halle.de

IWH List of Experts
The IWH List of Experts gives an overview of the IWH research themes. The institute's press office will be pleased to establish contact to the respective experts.

The Halle Institute for Economic Research (IWH) – Member of the Leibniz Association was founded in 1992. With its three research departments – Macroeconomics, Financial Markets, and Structural Change –, the IWH conducts economic research and provides economic policy recommendations, which are founded on evidence-based research. With the IWH's guiding theme "From Transition to European Integration", the institute's research concentrates on the determinants of economic growth processes with a focus on efficient capital allocation in a national and European context. Particular areas of interest for the institute are macroeconomic dynamics and stability, microeconomic innovation processes, productivity and labour markets, the dynamics of structural adjustment processes, financial stability and growth and the role of financial markets for the real economy.

The Leibniz Association connects 88 independent research institutions that range from the natural, engineering and environmental sciences via economics, spatial and social sciences to the humanities. Leibniz institutes address issues of social, economic and ecological relevance. They conduct knowledge-driven and applied basic research, maintain scientific infrastructure and provide research-based services. For further information see http://www.leibniz-gemeinschaft.de/en/home/.