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German economy will pick up speed only slowly

In winter of 2018/2019, the global economy weakened considerably, mainly due to economic policy risks. In Germany, the economy will pick up speed only slowly. According to IWH spring economic forecast, gross domestic product will increase by 0.5% in 2019. Growth in East Germany will amount to 0.7%.

Forecast for Germany: Key Economic Indicators[a] for Germany, 2017–2020

	2017	2018	2019	2020
	percentage change over previous year (price adjusted)			
Germany	2.2	1.4	0.5	2.0
East Germany[a]	1.9	1.4	0.7	1.7
	percentage change over previous year in %			
hours worked	1.3	1.4	0.9	0.9
hourly union wages	2.5	2.9	2.6	2.1
hourly actual wages	2.4	2.7	2.9	3.0
unit labour costs[b]	1.5	2.6	3.5	1.8
consumer price index	1.5	1.8	1.4	1.5
	1 000 persons			
employment (domestic)	44 269	44 838	45 251	45 609
unemployment[c]	2 533	2 340	2 188	2 044
	in %			
unemployment rate[d]	5.7	5.2	4.8	4.5
East Germany[a]	7.6	6.9	6.4	6.3
	in % of nominal GDP			
general government overall balance	1.0	1.7	1.0	0.9
current account balance	8.0	7.4	6.5	6.4

[a] East Germany including Berlin. – [b] Per hour (IWH calculations). – [c] Federal Employment Agency (BA) concept.– [d] Unemployment in % of civilian labour force (Federal Employment Agency (BA) concept).
Source: Federal Statistical Office; 2017–2020: IWH forecast (as of March 7, 2019).

In the winter half-year 2018/2019, the global economy has cooled off significantly. The economic development, however, diverges considerably between regions: the upturn in the USA has lost little momentum, while the recovery in the euro area has come to a standstill. The Chinese economy appears to be stumbling as well. One important reason for the slowdown in the global economy is the uncertainty surrounding the trade dispute between the United States on the one hand and China and the European Union on the other. For Europe, the unresolved Brexit negotiations put further strain on the economy. Although low interest rates and expansionary fiscal policies support the economy in the euro area, a sizeable pickup of the economy is likely to depend on further external stimulus, which might come when expansionary policy measures in China take effect in mid-2019.

In Germany, aggregate output stagnated in the final quarter of 2018, following a decline by 0.2% in the previous quarter. Problems of car producers adapting to a new emission gas test procedure, as well as the months-long failure of the Rhine as

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a waterway for the chemical industry, contributed to this weakness. More importantly, foreign demand, especially from the EU partner countries, has slowed down significantly. On the other hand, construction activity stays strong and companies continue building up employment, even, despite a decline in production, in the manufacturing sector. “Apparently, firms regard the current economic weakness as temporary, while the shortage of skilled workers is seen as a long-term problem. This has led, however, to a significant increase in unit labour costs”, says Oliver Holtemöller, head of the Department Macroeconomics and vice president at the Halle Institute for Economic Research (IWH). As a consequence, firms will not raise employment as fast as they did in 2018.

According to the IWH Flash Indicator production in the first half of 2019 will barely grow. Still, private consumption is likely to expand robustly, not least because real wages continue rising. In addition, low interest rates and discretionary fiscal policies, which will amount to 0.7% of GDP in 2019, will help. Real gross domestic product will be 0.5% higher in 2019 than in the previous year. In 2020, the growth rate will increase to 2.0%, partly due to more working days in that year. The East German economy expands by 0.7% in 2019 and by 1.7% next year.

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