Focus Germany

Lower GDP forecast – but domestic demand alive and kicking

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Germany: 2015 GDP forecast revised to 1.6% despite robust underlying momentum. The Q1 GDP details provide some comfort relative to the disappointing 0.3% qoq headline number. Final domestic demand was up 0.8% qoq while net-exports as well as inventories both provided a drag. Thus, our 2015 story of GDP growth driven by strong domestic demand remains intact. Despite this, we lower our 2015 GDP forecast from 2.0% to 1.6%. This is primarily due to the weaker-than-expected Q1 GDP growth that provides a lower starting base for 2015. However, we still expect quarterly growth rates to average a healthy 0.4% qoq in 2015. Despite softening in April and May ifo expectations and the composite PMI still point to 0.4%-0.5% qoq GDP growth for Q2. The details of the ifo report broadly confirm the domestic strength vs lack of external traction story. For now, we still expect global developments to provide a bit more momentum in H2, but the most recent business cycle data out of Germany have generally disappointed, raising question marks over the (external) momentum going into H2.

Construction investment: Sharp increase expected, but focus on downside risks. With leading indicators having reached record highs investment in construction should climb by 2.7% yoy in 2015 and 3.1% yoy in 2016 (in the wake of a 3.4% increase in 2014). Residential construction should remain the growth engine, expanding by over 3% in each of these two years, while commercial construction grows moderately. Given the plans for government spending programmes, to upgrade Germany's infrastructure in particular, we look for strong impetus from public construction. Some leading indicators point to a slowdown in construction growth. This might be partly driven by changes in the regulatory environment, particularly the introduction of the "Mietpreisbremse" (rent control), as well as capacity restrictions. If this trend continues, our baseline forecast could prove overly optimistic. The housing shortage in Germany's major cities and metropolitan regions is still the main feature of the German property market. A strong boost to construction investment would be needed to prevent further price increases.

The view from Berlin. German politics: Quarrel among friends and families. In Germany an increase in bickering within Chancellor Merkel's CDU/SPD coalition has even lead to speculation about its future. However, no-one is likely to be interested in early elections, given that a shift in the distribution of power in the Bundestag is unlikely. The populist AfD, last year's political shooting star, has its wings quarrelling over the party's course, so that a breakup may be looming. Although, the liberal FDP seems to be emerging from a crisis in new harmony, it is still doubtful whether the party's recovery will last.

Economic forecasts

	Real GDP (% growth)			Consumer Prices* (% growth)			Current Account (% of GDP)			Fiscal Balance (% of GDP)		
	2014F	2015F	2016F	2014F	2015F	2016F	2014F	2015F	2016F	2014F	2015F	2016F
Euroland	0.9	1.4	1.6	0.4	0.0	1.4	2.4	3.3	2.6	-2.4	-2.1	-1.7
Germany	1.6	1.6	1.7	0.9	0.3	1.5	7.6	8.0	7.8	0.6	0.6	0.7
France	0.2	1.1	1.6	0.6	0.1	1.1	-1.0	-0.5	-0.8	-4.0	-4.0	-3.4
Italy	-0.4	0.6	1.3	0.2	0.1	1.1	1.9	2.5	2.7	-3.0	-2.7	-2.2
Spain	1.4	2.8	2.4	-0.2	-0.6	1.5	0.8	1.4	1.0	-5.8	-4.5	-3.9
Netherlands	0.9	1.7	1.1	0.3	0.0	1.3	10.9	11.4	11.5	-2.3	-2.0	-1.9
Belgium	1.1	1.3	1.6	0.5	0.2	1.6	1.0	1.5	1.2	-3.2	-2.7	-2.2
Austria	0.3	1.2	1.8	1.5	0.7	1.7	0.7	1.2	1.5	-2.4	-1.6	-1.2
Finland	-0.1	0.8	1.4	1.2	0.1	1.3	-1.9	-1.5	-1.3	-3.2	-3.3	-2.8
Greece	0.7	0.8	3.2	-1.4	-1.6	1.0	1.0	1.5	1.2	-3.5	-0.7	-0.7
Portugal	0.9	1.6	1.6	-0.2	0.1	1.3	0.5	1.0	0.7	-4.5	-3.1	-2.5
Ireland	4.8	3.7	3.5	0.3	0.1	1.8	6.2	5.0	4.5	-4.1	-2.8	-2.5
UK	2.8	2.4	2.3	1.5	0.4	1.9	-5.3	-4.1	-2.9	-5.0	-4.0	-2.0
Denmark	1.1	1.7	1.8	0.6	1.0	1.5	6.2	6.0	6.0	-1.0	-2.5	-2.5
Norway	2.3	2.0	2.2	2.0	2.0	2.0	8.5	8.0	7.5	9.1	9.0	8.5
Sweden	2.3	2.8	2.8	-0.2	0.5	1.5	6.3	5.5	5.0	-1.9	-1.2	-0.6
Switzerland	2.0	1.0	1.0	0.0	-0.8	-0.4	8.0	8.5	8.5	0.2	0.5	0.5
Czech Republic	2.0	2.7	2.5	0.4	0.5	2.0	0.6	0.2	0.0	-1.9	-1.8	-1.6
Hungary	3.6	2.7	2.4	-0.2	-0.1	2.6	3.9	3.0	3.1	-2.6	-2.7	-2.4
Poland	3.3	3.4	3.5	0.0	-0.6	1.4	-1.4	-1.6	-1.7	-3.4	-2.9	-2.7
United States	2.4	2.4	3.0	1.6	0.2	2.5	-2.6	-3.0	-3.6	-2.8	-2.7	-2.4
Japan	-0.1	0.8	1.8	2.7	0.8	0.9	0.5	2.8	2.6	-5.9	-5.4	-4.5
China	7.4	7.0	6.7	2.0	1.8	2.7	3.1	3.4	3.3	-2.1	-3.0	-3.0
World	3.4	3.3	3.8	3.6	3.3	3.8						

*Consumer price data for European countries based on harmonized price indices except for Germany. This can lead to discrepancies compared to other DB publications.
Sources: National Authorities, Deutsche Bank

Forecasts: German GDP growth by components, % qoq, annual data % yoy

						2014				2015			
	2012	2013	2014	2015F	2016F	Q1	Q2	Q3	Q4	Q1	Q2F	Q3F	Q4F
Real GDP	0.4	0.1	1.6	1.6	1.7	0.8	-0.1	0.1	0.7	0.3	0.4	0.5	0.3
Private consumption	0.7	0.8	1.1	2.1	1.0	0.8	0.0	0.7	0.7	0.6	0.3	0.4	0.3
Gov't expenditure	1.2	0.7	1.2	1.7	0.4	0.0	0.7	0.6	0.3	0.7	0.1	0.3	0.2
Fixed investment	-0.7	-0.6	3.3	2.8	2.7	3.0	-1.7	-1.2	0.8	1.5	0.0	1.5	0.8
Investment in M&E	-3.1	-2.4	4.3	3.9	3.7	2.0	0.6	-1.4	0.4	1.5	0.5	2.0	1.0
Construction	0.6	-0.1	3.4	2.7	3.1	4.5	-3.7	-1.5	1.3	1.7	-0.4	1.8	0.9
Inventories, pp	-1.4	0.2	-0.3	-0.2	0.1	-0.2	-0.1	-0.5	0.4	-0.3	0.1	0.1	0.0
Exports	2.8	1.6	3.8	4.7	5.0	0.1	1.0	1.5	1.0	0.8	1.0	1.0	1.2
Imports	0.0	3.1	3.5	5.8	4.4	0.2	0.7	0.8	1.9	1.5	0.9	1.5	1.5
Net exports, pp	1.3	-0.5	0.4	0.0	0.4	-0.1	0.2	0.4	-0.3	-0.2	0.1	-0.1	-0.1
Consumer prices*	2.0	1.5	0.9	0.3	1.5	1.2	1.1	0.8	0.5	0.0	0.2	0.5	0.8
Unemployment rate, %	6.8	6.9	6.7	6.5	6.5	6.8	6.7	6.7	6.6	6.5	6.4	6.4	6.5
Industrial production	-0.4	0.1	1.5	1.7	2.2								
Budget balance, % GDP	0.1	0.1	0.6	0.6	0.7								
Public debt, % GDP	79.0	76.9	73.3	69.6	66.0								
Balance on current account, % GDP	6.8	6.5	7.6	8.0	7.8								
Balance on current account, EUR bn	187	182	220	239	244								

*Inflation data for Germany based on national definition. This can lead to discrepancies to other DB publications.
Sources: Federal Statistical Office, German Bundesbank, Federal Employment Agency, Deutsche Bank Research

Germany: 2015 GDP forecast revised to 1.6% despite robust underlying momentum

— The Q1 GDP details provide some comfort relative to the disappointing 0.3% qoq headline number. Final domestic demand was up 0.8% qoq and net-exports as well as inventories both provided a drag. Thus, our 2015 story of GDP growth driven by strong domestic demand remains intact.

— Despite this, we lower our 2015 GDP forecast from 2.0% to 1.6%. This is primarily due to the weaker-than-expected Q1 GDP growth that provides a lower starting base for 2015. However, we stwill expect quarterly growth rates to average a healthy 0.4% qoq in 2015.

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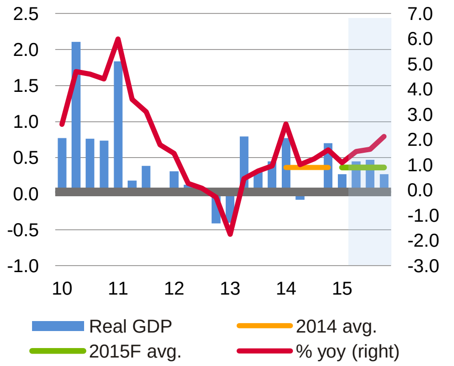
Quarterly GDP growth in 2015 same as 2014 — 1

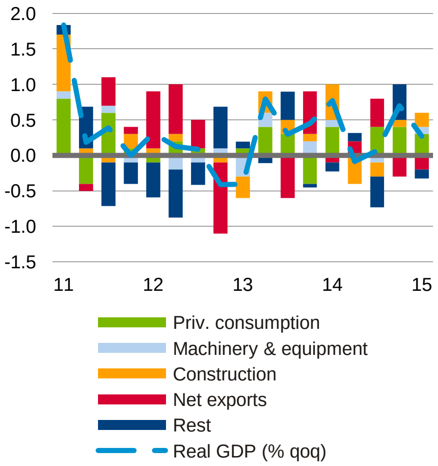
Real GDP, % qoq



Sources: Federal Statistical Office, Deutsche Bank Research

Private consumption boosted growth lately — 2

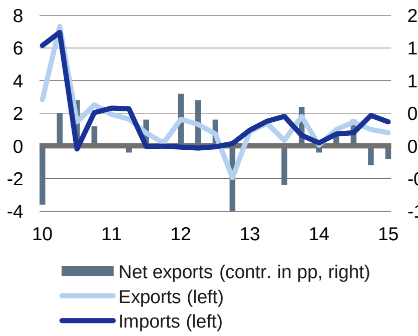
Contribution to real GDP growth, qoq, pp



Sources: Federal Statistical Office, Deutsche Bank Research

Imports outpaced exports lately — 3

Real, sa, % qoq



Source: Federal Statistical Office

Q1 GDP data: Domestic cycle remained strong

The Q1 GDP data provide some comfort relative to the disappointing headline GDP reading and continue to support our 2015 story of GDP growth driven by strong domestic demand. Headline GDP growth slowed to a disappointing +0.3% qoq (vs +0.7% qoq prev., Reuters Consensus range +0.4% - +0.9%).

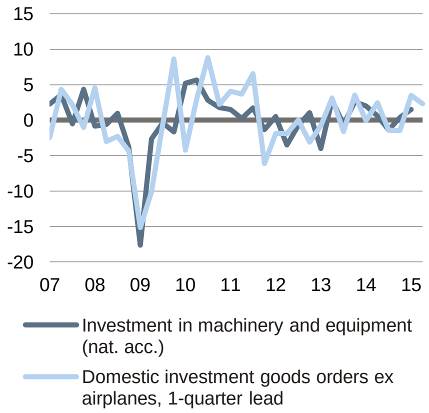
Net exports weighed on growth (-0.2% percentage points). This was the second consecutive quarter bringing a drag from this side (Q4 2014: -0.3% pp) as imports (+1.5% qoq) rose again by about double the pace of exports (+0.8% qoq). Overall, while exports are rising by less than in past cycles they were still up by 4.3% yoy in Q1 – on track to meet our full year forecast. Export growth is limited by weak global trade and marked by a divergence between demand from developed markets (strength in the US and improvement in EMU) and developing markets (Russia in recession, China weakening). Imports were up a stronger 5.0% yoy – a sign of the domestic strength especially in consumption. The drop in oil prices provided an additional fillip to real imports. This effect should dissipate over the rest of the year.

In our view, the main surprise was the ongoing drag from inventories. They lowered growth by 0.3 pp. Inventories were negative in all but one of the last 5 readings. We are always cautious about over-interpreting this component since – in contrast to the US – it is not based on data, but is the residual item between the production and expenditure side of national accounts and is often heavily revised. For instance, the negative Q4 reading was revised from -0.2 pp to +0.4 pp. One could argue that businesses still remain cautious with regard to future demand and are keeping inventories lean. This explanation is somewhat unsatisfactory, though, given domestic strength and the overall robust pace of foreign demand. The ifo and PMI data on inventories, in our view, do not suggest that companies see a big problem with inventories in either direction.

By contrast, domestic demand remained very healthy. Final domestic demand was up 0.8% qoq in Q1 and averaged +0.6% qoq over the last three quarters and +0.5% qoq over the last five quarters. In Q1 domestic demand growth was broadly based with private consumption barely losing any momentum (+0.6% vs +0.7% prev.). While nominal disposable incomes stagnated after substantial growth in previous quarters, the savings rate declined again in Q1 (9.4%) after it had risen strongly in Q4 (9.8%) likely on the back of surprising savings due to

Slower equipment investment in Q2 likely 4

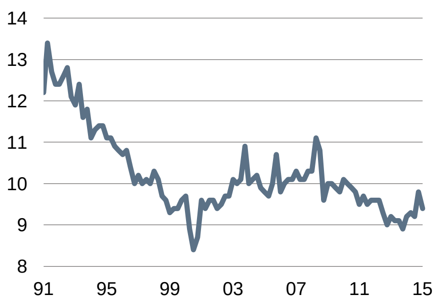
Real, % qoq



Source: Federal Statistical Office

Savings rate: Down again from high Q4 level 5

%, sa



Source: Federal Statistical Office

the oil price decline. This suggests that this stimulus to real disposable income has now largely found its way into consumption spending. Government consumption accelerated (+0.7% qoq vs +0.3% prev.). Construction investment was up somewhat less (+1.7% qoq vs +1.3%) than monthly indicators had suggested. The two consecutive strong readings still provide a very solid starting base for full-year construction growth, although it was somewhat overstated due to the mild winter. Investment in machinery & equipment (+1.5% vs +0.4% prev.) was robust, achieving the highest rate of the last four quarters. It is unlikely to point to the start of a strong investment cycle as domestic investment goods orders have slowed again lately as demand for German industrial goods is not strong enough to bring capacity utilisation substantially above its historical average.

2015 GDP revised to 1.6%, but healthy quarterly growth

We lower our 2015 GDP forecast from 2.0% to 1.6%. This is primarily due to the weaker-than-expected Q1 GDP growth that provides a lower starting base for 2015. However, we still expect quarterly growth rates to average a healthy 0.4% qoq in 2015 – this is about the same average that we had expected when increasing our GDP forecast to 2% in February and this was also the average in 2014. We expect GDP growth to pick up slightly to +0.4% in Q2F as net exports and inventories stop being a drag and other components continue their solid growth, which would be about in line with the ifo and PMI levels in Apr./May.

The downward revision should not distract from the underlying story of strong domestic demand that remains unchanged in our view. From a growth composition perspective our forecast is now even further tilted toward domestic demand as we now see net exports making a neutral contribution to growth as imports (2015F: +5.8%) outpace exports (+4.7%) even more than previously forecast. This is in line with DB's global 2015 GDP growth forecast, which has now been lowered from 3.4% to 3.3%, and global trade that has remained lacklustre. Otherwise we continue to expect private consumption to grow at over 2% (2.1%; government consumption: +1.7%). Investment should also be healthy with machinery & equipment expanding by 3.9% helped by a base effect. Construction might grow by 2.7% in 2015 (for details see the following article).

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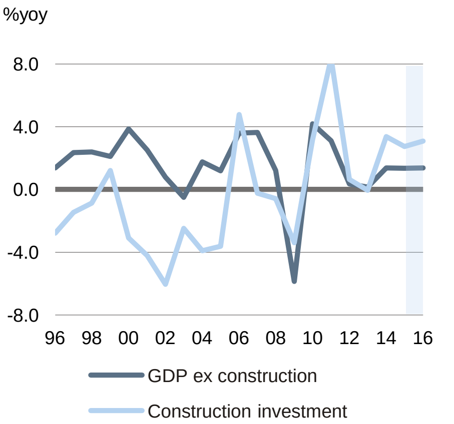
Construction investment: Sharp increase expected, but focus on downside risks

— With leading indicators having reached record highs investment in construction should climb by 2.7% yoy in 2015 and 3.1% yoy in 2016 (in the wake of a 3.4% increase in 2014). Residential construction should remain the growth engine, expanding by over 3% in each of these two years, while commercial construction grows moderately. Given the plans for government spending programmes, to upgrade Germany's infrastructure in particular, we look for strong impetus from public construction.

— Some leading indicators point to a slowdown in construction growth. This might be partly driven by changes in the regulatory environment, particularly the introduction of the "Mietpreisbremse" (rent control), as well as capacity restrictions. If this trend continues, our baseline forecast could prove overly optimistic.

— The housing shortage in Germany's major cities and metropolitan regions is still the main feature of the German property market. A strong boost to construction investment would be needed to prevent further price increases. If the downside risks to investment in residential construction materialise there is a danger of the price pressure intensifying on account of an even larger supply bottleneck.

GDP growth & construction investment 1



Sources: Destatis, Deutsche Bank Research

Despite the unbroken upswing in the real estate market since 2009, construction investment has grown only moderately at around 3% per year. This corresponds to a relatively low price elasticity of only about ½, since prices have climbed by roughly 6% per year. This expansion of construction investment started from a low level. As a percentage of gross domestic product, German construction investment is relatively low both by historical and international standards.

The modest expansion of supply has exacerbated the housing scarcity in Germany's major cities and metropolitan regions. Since the demand for real estate is set to continue to grow dynamically for the time being, a pronounced jump in construction investment will be needed to alleviate the supply bottleneck. Accordingly, construction investment is also of key importance to future price trends in the property market. Our investment forecasts are based on the following main arguments: 1. the continuation of the current real estate cycle, 2. the leading indicators and 3. capacity restrictions on building output and the change in the regulatory environment.

Demand overhang in current property upswing buoys construction investment

Real estate cycles often last several years, and very long cycles can persist for several decades in fact. Correspondingly, with a duration of six years the upswing in the cycle that began in Germany in 2009 is nearly spot on the historical international average. The fact that there are very strong incentives for tenants to purchase real estate in the current low interest rate environment suggests the cycle will continue for a long time. For many tenants the interest and repayment charges currently incurred on the purchase of a home are lower than the rent. Especially Germany, with its very low home-ownership ratio, could see the current cycle continue for several more years. As a result, Germany's home-ownership ratio could skyrocket.

This possibility is also backed by the fact that house prices started to return to normal over the past six years. They climbed by nearly 50% in the major cities and 30% country-wide, while office prices picked up by over 20%. By international standards, this may be regarded as an average property upswing. Besides, it started from pretty low levels. In its last quarterly report the central bank of Austria said it continued to view the German housing market as being undervalued.[1] This supports the argument that German real estate prices are still cheap in an international comparison and the normalisation process should continue. Another reason the cycle should continue is that the macroeconomic environment provides positive stimuli. The increase in employment is set to continue thanks to immigration, and we look for GDP growth of 1.6% for 2015 and 1.7% for 2016. As in 2014, this market and macroeconomic environment ought to be reflected in higher construction investment.

Construction indicators: High levels, but slowing growth

Forecast: Construction investment 2

% yoy	2014	2015	2016
Residential	3.8	3.3	4.4
Commercial	2.2	1.4	1.1
Public	4.0	0.0	3.0
Total	3.4	2.7	3.1

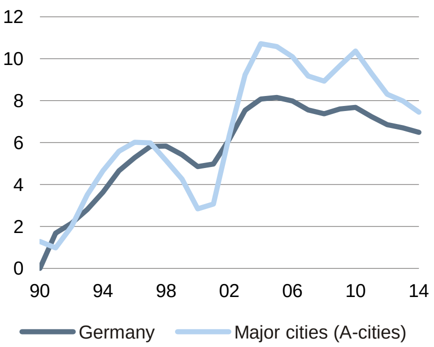
Source: Deutsche Bank Research

Construction indicators such as new orders, order books, building permits, sales per year, employment and the ifo construction index have picked up noticeably over the past six years and are now at high levels (charts 5-12). The sizeable order backlog and pronounced increase at end-2014 in particular continue to imply rising construction investment in 2015. True, some indicators point to easing growth, but given in some cases long lead times and the high indicator levels we expect a 2.7% expansion of construction investment in 2015 and 3.1% in 2016, in the wake of a 3.4% increase in 2014 (chart 2).

Following the weather-induced surge in Q1 2015 (1.7% qoq), we expect to see a compensatory effect in Q2 (-0.5%). This forecast is partly based on the slowing momentum of the ifo indicators. For the year as a whole, construction investment growth should continue to be driven by the residential segment, which should pick up by over 3% in each of these two years. Because of a pronounced negative growth overhang from 2014 commercial construction performance is likely to be below average with expansion of 1.4% yoy, and only 1.1% in the following year. The weaker growth in the commercial segment is also reflected in a modest increase in office workers relative to the number of employees required to pay social security contributions. Accordingly, the supply overhang and vacancy rates in the office market that have existed for years are falling only slowly. In 2014, the office vacancy rates in the major cities fell to roughly 7%, while they still hovered around 10.4% in 2010. By comparison: the vacancy rates in the housing market are often far below 2% (charts 3 and 4).

Office market: Vacancy rate 3

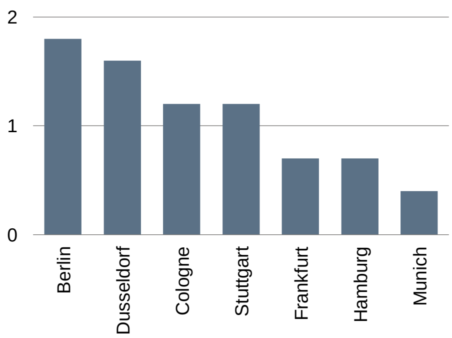
% of total office stock



Sources: BulwienGesa, Deutsche Bank Research

Dwellings: Marketable vacancy rate 4

% of total building stock per city



Sources: CBRE, Deutsche Bank Research

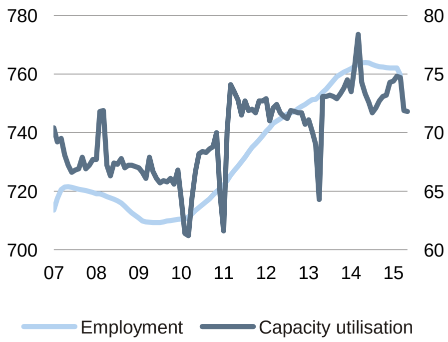
[1] "Calculating this indicator with data for Germany we see an undervaluation of 7% in Q3/14". MONETARY POLICY & THE ECONOMY. Quarterly Review of Economic Policy. Q1/15. Housing Markets in Austria, Germany and Switzerland. Martin Schneider and Karin Wagner.

We expect public construction to stage a strong recovery in the course of 2015 following a significant decline in the first quarter (-3% qoq). Nonetheless, the Q1 downturn neutralises the sizeable growth overhang from the previous year along with the extremely positive new order trend at the start of the year in our forecast, meaning that investment in public construction will be flat for the year as a whole. In 2016 it is likely to increase by 3%. This forecast is not based on a model estimate, though, but on the assumption that the current debate over deficiencies in German infrastructure will lead to additional investment. In March, the federal government announced the main points of an investment initiative that will channel an additional EUR 10 bn into public transport infrastructure and measures to boost energy efficiency, digital infrastructure, climate protection and urban development from 2016 to 2018.

Ultimately, the price pressure in the current real estate cycle will not ease until the supply bottleneck is alleviated via a very strong expansion of construction investment. Even in the baseline scenario with a substantial increase in investment as depicted here this imbalance is likely to be run down only slowly over a period of several years. The current cycle should continue, with real estate prices climbing further, rental yields far outstripping the financing costs and thus also sending the price signals that will lead to further investment in construction.

Employment 5

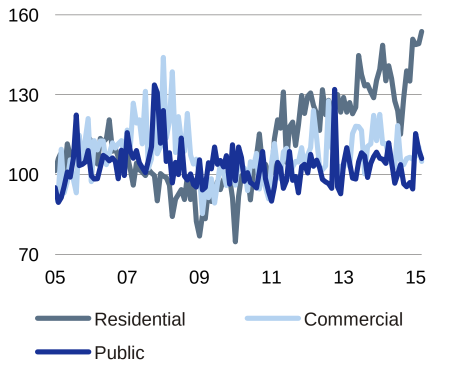
Left axis: employed persons in '000, 12M mov. avg.
Right axis: capacity utilisation in %



Sources: Destatis, Deutsche Bank Research

New orders 6

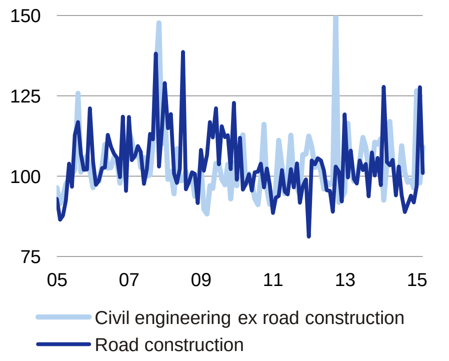
2010=100
working-day and seasonally adjusted



Sources: Destatis, Deutsche Bank Research

New orders: Public 7

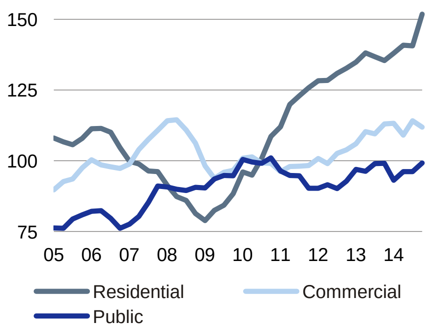
2010=100
working-day and seasonally adjusted



Sources: Destatis, Deutsche Bank Research

Order book 8

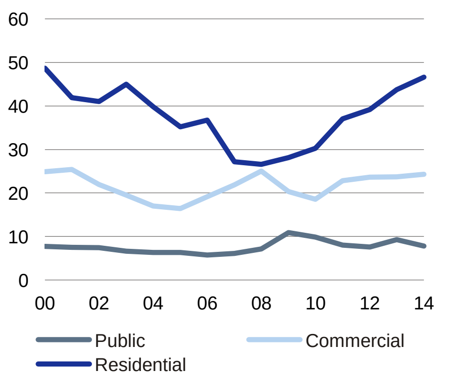
2010=100
working-day and seasonally adjusted



Sources: Destatis, Deutsche Bank Research

Building permits per year 9

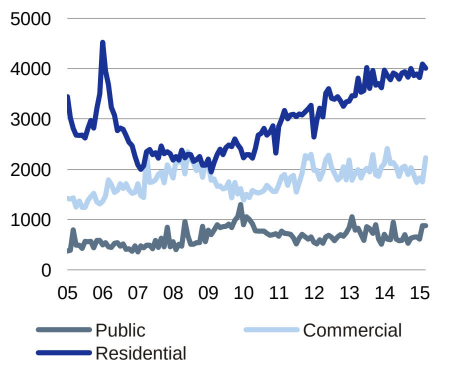
Reported costs, EUR bn



Sources: Destatis, Deutsche Bank Research

Building permits per month 10

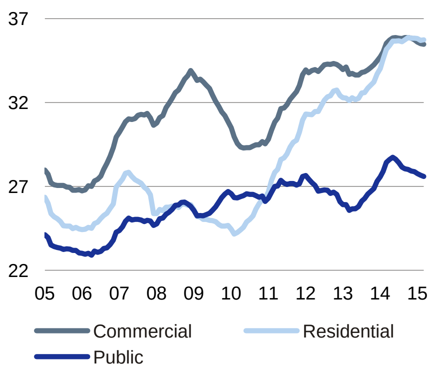
Reported costs, EUR m



Sources: Destatis, Deutsche Bank Research

Sales per year 11

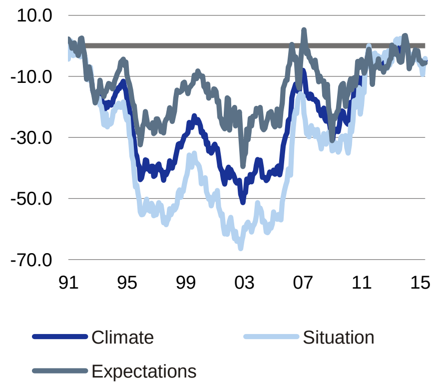
EUR bn, 12M moving average



Sources: Destatis, Deutsche Bank Research

ifo construction index 12

Net percentage balance, sa



Sources: ifo, Deutsche Bank Research

Downside risks due to regulatory environment and capacity restrictions

The growth momentum of several leading indicators has eased over the past few months. One example worth mentioning in particular is building permits, which are trending sideways in the residential and commercial segments after having at times shown double-digit percentage growth in previous years. The ifo construction index, sales in the public segment and new order intake in the commercial segment are slightly decreasing in fact.

Potential reasons for the muted construction growth are the regulatory environment and capacity restrictions on building output. Capacity utilisation in the sector has hit record highs, meaning that a further expansion of supply would be linked with high costs and therefore no action is being taking. Moreover, the ifo Institute says a relatively large number of building firms report a shortage of workers, and the Federal Employment Agency a shortage of skilled tradespeople in the plumbing and sanitary fittings sector in particular. The number of vacancies for this group of workers that is obliged to pay social security contributions continues to surge and the number of job vacancies far exceeds the number of jobseekers. Bottlenecks in subsectors could curb building activity as a whole. Since the apprenticeship figures in construction are in fact declining slightly, the shortage of skilled workers could become chronic. Furthermore, the large number of applications to draw a pension at 63 (roughly 280,000 at the end of March) may further exacerbate the shortage in the sector.

The change in the regulatory environment could be another cause of the limited momentum seen with some leading indicators. The debate about "affordable housing" that began with the federal election campaign in mid-2013 presumably heightened investor uncertainty about the future regulatory environment. It remained unclear until recently just how the new law would regulate newbuild housing and the modernisation of existing stock. Construction-sector investors may have postponed some projects in order to await the impact of the new rules on their investment models. Also, the possibility looms that constitutional complaints may be filed against rent control. Equally, the lack of legal underpinning for the calculation of “usual local rent levels” could lead to legal squabbles – according to the new law, the rent charged when re-letting existing stock must not exceed 10% of the usual local level at the maximum. In May 2015, a district court in Berlin classified the local rent index ("Mietspiegel") as unscientific and thus questioned its use as a basis for legislation. These uncertainties surrounding the issue of rent control could also dampen capitalintensive expansion investment in cranes, building machinery and construction vehicles.

Given the introduction of rent control – in a market that is already heavily regulated anyway – and the possibility of capacity restrictions it follows that our construction investment forecasts are faced with downside risks.

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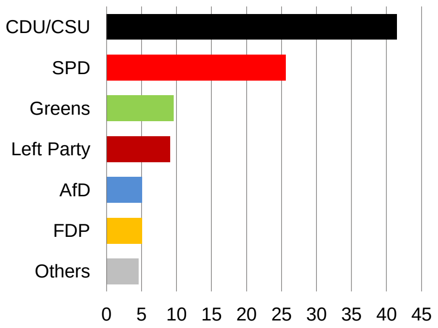
The View from Berlin

Popularity of major parties in DE, according to the Allensbach survey 1

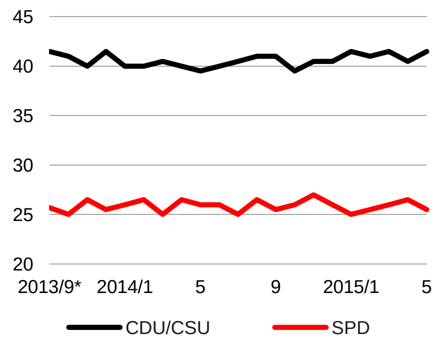
As of mid-May, %



Source: IfD Allensbach

Lasting difference in the popularity of the CDU/CSU and the SPD 2

%

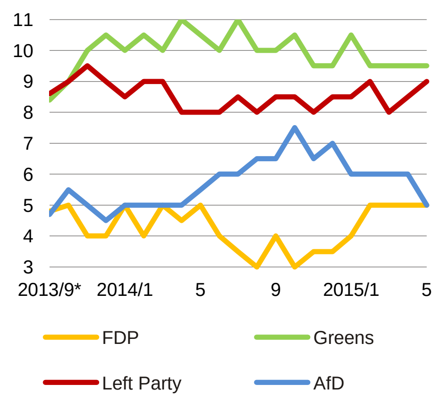


* Result of the federal election on September 22

Sources: Wahlrecht.de; IfD Allensbach

Smaller parties' popularity over time 3

%



* Result of the federal election on September 22

Sources: Wahlrecht.de; IfD Allensbach

German politics: Quarrels among friends and families

In Germany an increase in bickering among political actors and parties has attracted growing public attention. In Chancellor Merkel's governing coalition a debate on the cooperation between the German intelligence service BND and its US counterpart, the NSA, has escalated. Some commentators are already wondering if the coalition will hold. The populist AfD, last year's political shooting star, has its divergent political wings quarrelling over the party's course. The liberal FDP, by contrast, seems to be emerging from its crisis in new harmony.

The hefty debate among the government parties is astonishing, given that according to a recent survey 70% of the Germans think they are not affected by the BND's activities. Thus, the debate is seen as a sign of deterioration in Berlin's political climate. In fact, business-friendly CDU/CSU MEPs feel that the coalition's work has hitherto been biased, with the government mainly implementing the SPD's favourite projects, such as the minimum wage and the pension at 63, while their calls, e.g. income tax cuts, have not yet been heeded. The SPD is unhappy with its weak approval ratings of 25-26%, while the CDU/CSU frequently polls about 41%, due largely to Mrs. Merkel's popularity.

Countering the SPD leader Gabriel's demand that chancellor Merkel should demonstrate more political "backbone" in the BND/NSA issue, a vice-chairman of the CDU's parliamentary group has now even hinted at the possibility of a snap election. At present, however, none of Germany's major parties are likely to be interested in early elections. Markets were therefore right not to react to the statement from the CDU MP. The coalition still has important projects pending, especially the energy transition and the reform of the tax revenue equalisation scheme. To pass the respective legislation a consensus between the CDU/CSU and the SPD would be imperative, even if they were not coalition partners. Furthermore, at present, there is no prospect of a fundamental shift in the distribution of power in favour of one of the two camps.

Recently, new uncertainty has resulted from the unclear fate of the AfD. The party's liberal conservative wing and its right wing are involved in a power struggle. Economics professor Lucke, who founded the party 2½ years ago as a club of critics of the EU's euro bailout policy, has already asked his followers to join a new movement. Although the latter does not (yet) have the status of a political party, a break-up of the AfD is looming. But neither Lucke's decimated eurosceptics nor a presumably right-wing and primarily Eastern Germany-based rump AfD would be a force to be reckoned with at the federal level.

By contrast, the FDP is recovering from the heavy election defeats it suffered in the past few years. At its recent party conference the FDP celebrated its new leadership team as well as respectable results at two recent Länder elections in Hamburg and Bremen and demonstrated new harmony. But despite improvements in recent polls, too, it is still very doubtful whether the FDP will be able to clear the 5% threshold at the next general election, be it in autumn 2017 – as scheduled – or in the unlikely event of an earlier election.

A continuing recovery of the FDP would provide the CDU/CSU with a further option to form a new coalition in autumn 2017. The SPD lacks an alternative to the present coalition as long as its popularity rating together with that of the Greens and the Left party remain below 45% in total. Although these two smaller parties have not produced negative headlines recently, their approval ratings are hovering around 10% and 9%, respectively.

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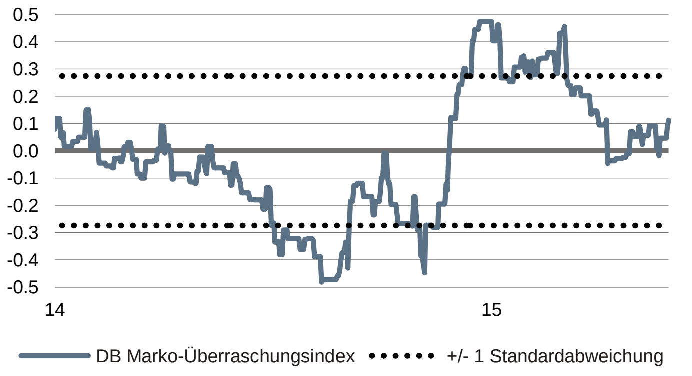
DB German Macro Surprise Index

The DB German Macro Surprise Index compares published economic data with market forecasts and thus provides clues as to the direction of future forecast revisions.[2]

DB German Macro Surprise Index

Average of last 20 z-scores of data surprises

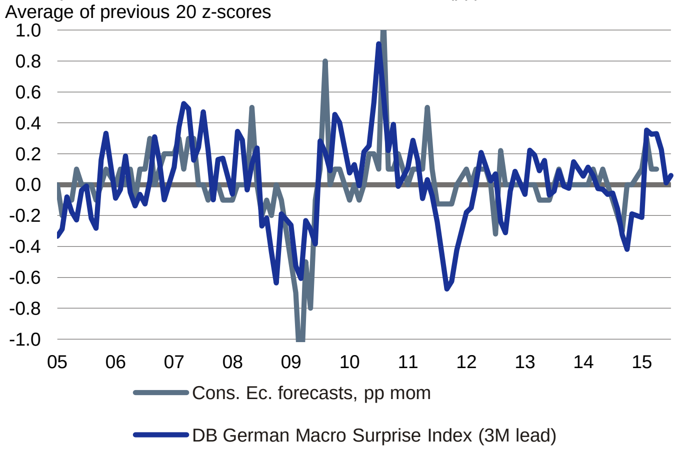


Values above (below) 0 indicate the data came in better (worse) than expected

Sources: Bloomberg Finance LP, Deutsche Bank Research

DB German Macro Surprise Index and revisions of Consensus GDP forecasts

Monthly revisions of Consensus Economic Forecasts (pp); Average of previous 20 z-scores



Sources: Consensus Economics Inc., Deutsche Bank Research

Last 20 published economic data for Germany

Bloomberg Tickers	Indicator	Reporting month	Publication date	Current value	Bloomberg consensus	Surprise	Standardised surprise	Quantile rank
GRZEWI Index	ZEW Survey Expectations	4 2015	21.04.15	53.3	55.3	-2.0	-0.2	0.4
GRZECURR Index	ZEW Survey Current Situation	4 2015	21.04.15	70.2	56.5	13.7	1.8	1.0
GRIFPBUS Index	IFO Business Climate	4 2015	24.04.15	108.6	108.4	0.2	0.0	0.5
GRIMP95Y Index	Import Price Index (% yoy)	3 2015	27.04.15	-1.4	-2.0	0.6	0.8	0.9
GRFRIAMM Index	Retail Sales (% mom)	3 2015	30.04.15	-1.4	0.5	-1.9	-1.2	0.1
GRUECHNG Index	Unemployment Change (000's mom)	4 2015	30.04.15	-8.0	-15.0	-7.0	-0.5	0.3
MPMIDEMA Index	Markit Manufacturing PMI	4 2015	04.05.15	52.1	51.9	0.2	0.2	0.6
MPMIDESA Index	Markit Services PMI	4 2015	06.05.15	54.0	54.4	-0.4	-0.4	0.3
GRIORTMM Index	Factory Orders (% mom)	3 2015	07.05.15	0.9	1.5	-0.6	-0.3	0.4
GRIPIMOM Index	Industrial production (% mom)	3 2015	08.05.15	-0.5	0.4	-0.9	-0.7	0.2
GRCAEU Index	Current Account Balance (EUR bn)	3 2015	08.05.15	27.9	20.0	7.9	2.0	1.0
GRCP20YY Index	CPI (% yoy)	4 2015	13.05.15	0.5	0.4	0.1	0.8	0.8
GRZEWI Index	ZEW Survey Expectations	5 2015	19.05.15	41.9	49.0	-7.1	-0.8	0.2
GRZECURR Index	ZEW Survey Current Situation	5 2015	19.05.15	65.7	68.0	-2.3	-0.4	0.3
MPMIDESA Index	Markit Services PMI	5 2015	21.05.15	52.9	52.9	0.0	0.0	0.5
MPMIDEMA Index	Markit Manufacturing PMI	5 2015	21.05.15	51.4	51.4	0.0	0.0	0.5
GRGDPPGQ Index	GDP (% qoq)	3 2015	22.05.15	0.3	0.3	0.0	-0.1	0.3
GRIFPBUS Index	IFO Business Climate	5 2015	22.05.15	108.5	108.3	0.2	0.0	0.5
GRIMP95Y Index	Import Price Index (% yoy)	4 2015	28.05.15	-0.6	-0.7	0.1	0.4	0.7
GRFRIAMM Index	Retail Sales (% mom)	4 2015	29.05.15	1.7	1.0	0.7	0.8	0.8

Sources: Bloomberg Finance LP, Deutsche Bank Research

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[2] See for details Focus Germany. August, 4 2014.

Germany: Events of economic-, fiscal- and euro-politics

Date	Event	Remarks
3 June	ECB Governing Council meeting, press conference	The Council is fully committed to the QE programme to purchase EUR 60 bn of securities per month until September 2016 and possibly beyond.
7 to 8 June	G7 leaders summit, Kruen/Elmau (Bavaria)	Global economy, foreign, security and development policy, climate protection, energy security among others.
16 June	European Court of Justice (ECJ), Luxembourg	ECJ judges over the ECB's OMT programme. In principle, the judgment will be binding for the German Constitutional Court (GCC) and its future judgment on pending constitutional complaints against OMT. The ECJ will most likely hold that OMT complies with the European Treaties. However, it remains to be seen whether the German Court will thoroughly follow the ECJ's judgment. Even if OMT was limited in scope, the ECB will be able to calm sovereign bond markets with QE action.
18 to 19 June	Eurogroup and ECOFIN meeting, Brussels	Among others European semester – discussion on SCPs and euro area specific recommendations, Greece, Eurogroup work programme for H2 2012.
25 to 26 June	European Council meeting, Brussels	Debate on the nature and structure of the euro area on the basis of the Four Presidents' Report, and on the EU's strategy for foreign and security policy and possibly on the situation in Greece.
13 to 14 July	Eurogroup and ECOFIN meeting, Brussels	Possibly Greece and the situation in the euro area among others.
16 July	ECB Governing Council meeting, press conference	The risk of an early reconsideration of the QE programme is low.

Source: Deutsche Bank Research

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Germany: Data calendar

Date	Time	Data	Reporting period	DB forecast	Last value
1 June 2015	14:00	Consumer prices preliminary (Index, sa), pch mom (yoy)	May	0.1 (0.7)	0.0 (0.5)
2 June 2015	10:00	Unemployment rate (%, sa)	May	6.4	6.4
5 June 2015	8:00	New orders manufacturing (Index, sa), pch mom	April	0.5	0.9
8 June 2015	8:00	Industrial production (Index, sa), pch mom	April	0.2	-0.5
8 June 2015	8:00	Trade balance (EUR bn, sa)	April	18.7	19.4
8 June 2015	8:00	Merchandise exports (EUR bn, sa), pch mom (yoy)	April	0.2 (5.7)	1.3 (8.4)
8 June 2015	8:00	Merchandise imports (EUR bn, sa), pch mom (yoy)	April	1.1 (5.4)	2.4 (4.7)
23 June 2015	9:30	Manufacturing PMI (Flash)	June	51.2	51.4
23 June 2015	9:30	Services PMI (Flash)	June	53.2	52.9
24 June 2015	10:30	ifo business climate (Index, sa)	June	108.5	108.5
29 June 2015	8:00	Import prices (Index, sa) pch mom (yoy)	May	0.2 (-0.4)	0.6 (-0.6)
2 July 2015	8:00	Retail sales (Index, sa), pch mom	May	-0.5	1.7
14 Aug 2015	8:00	Real GDP (Index, sa), % qoq	Q2 2015	0.4	0.3

Sources: Deutsche Bank Research, Federal Statistical Office, Federal Employment Agency, ifo, Markit

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Financial Forecasts

	US	JP	EMU	GB	CH	SE	DK	NO	PL	HU	CZ
Key interest rate, %											
Current	0.120	0.10	0.05	0.50	-1.25	-0.25	0.05	1.25	1.50	1.65	0.05
Jun 15	0.125	0.10	0.05	0.50	-0.75	-0.25	0.05	1.25	1.50	1.50	0.05
Dec 15	0.625	0.10	0.05	0.50	-0.75	-0.25	0.05	1.00	1.50	1.50	0.05
Mar 16	0.875	0.10	0.05	0.50	-0.75	-0.25	0.05	1.00	1.50	1.60	0.05
3M interest rates, %											
Current	0.26	0.20	-0.01	0.57							
Jun 15	0.26	0.15	0.00	0.58							
Dec 15	0.75	0.15	-0.10	0.59							
Mar 16	1.18	0.15	-0.10	0.60							
10Y government bonds yields, %											
Current	2.12	0.53	0.54	1.84							
Jun 15	2.00	0.40	0.60	1.85							
Dec 15	2.45	0.55	0.70	2.15							
Mar 16	3.35	0.60	0.80	2.35							
Exchange rates											
	EUR/USD	USD/JPY	EUR/GBP	GBP/USD	EUR/CHF	EUR/SEK	EUR/DKK	EUR/NOK	EUR/PLN	EUR/HUF	EUR/CZK
Current	1.09	123.70	0.71	0.65	1.03	9.25	7.46	8.49	4.13	308.65	27.46
Jun 15	1.04	121.00	0.72	1.44	1.07	9.20	7.46	8.90	3.97	292.56	27.50
Dec 15	1.00	125.00	0.74	1.36	1.10	8.90	7.46	9.00	4.08	285.00	27.50
Mar 16	0.98	126.25	0.74	1.33	1.10	8.86	7.46	8.95	4.06	300.00	27.50

Sources: Bloomberg, Deutsche Bank

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German data monitor

	Q2 2014	Q3 2014	Q4 2014	Q1 2015	Q2 2015	Dec 2014	Jan 2015	Feb 2015	Mar 2015	Apr 2015	May 2015
Business surveys and output											
Aggregate											
Ifo business climate	110.0	106.7	104.7	107.1		105.6	106.7	106.8	107.9	108.6	108.5
Ifo business expectations	105.4	101.9	100.3	102.8		101.4	101.9	102.5	103.9	103.4	103.0
Industry											
Ifo manufacturing	106.2	102.8	99.9	102.8		101.2	102.2	102.3	103.8	104.5	104.3
Headline IP (% pop)	-1.1	0.0	0.8	0.5		1.0	-0.1	0.0	-0.5		
Orders (% pop)	-1.0	1.3	1.4	-1.6		3.3	-2.7	-0.9	0.9		
Capacity Utilisation	84.0	83.8	84.1	84.5	84.9						
Construction											
Output (% pop)	-4.9	0.4	1.4	1.9		1.4	1.1	-2.6	4.5		
Orders (% pop)	-4.5	-2.4	-0.1	8.6		1.0	9.8	-1.6	-2.2		
Ifo construction	119.8	120.4	120.4	118.8		119.6	119.3	119.2	118.0	119.5	119.7
Consumer demand											
EC consumer survey	4.3	1.0	-1.2	1.0		-1.4	0.0	-0.1	3.2	3.3	3.0
Retail sales (% pop)	0.0	0.0	1.7	1.0		0.9	0.8	-0.2	-1.4	1.7	
New car reg. (% yoy)	-0.3	4.1	2.7	6.4		6.7	2.6	6.6	9.0	6.3	
Foreign sector											
Foreign orders (% pop)	-1.0	3.4	0.9	-3.3		3.0	-3.4	-1.7	-1.6		
Exports (% pop)	0.5	2.4	1.4	0.6		2.8	-2.1	1.4	1.3		
Imports (% pop)	-0.9	0.6	0.5	1.4		-0.7	-0.2	1.3	2.4		
Net trade (sa EUR bn)	52.2	57.5	60.3	59.0		21.5	19.7	20.0	19.4		
Labour market											
Unemployment rate (%)	6.7	6.7	6.6	6.5		6.5	6.5	6.5	6.4	6.4	
Change in unemployment (k)	-20.0	-0.7	-37.3	-48.0		-25.0	-9.0	-19.0	-14.0	-8.0	
Employment (% yoy)	0.9	0.8	0.9	0.7		0.9	0.8	0.6	0.6		
Ifo employment barometer	106.8	106.5	106.4	107.7		106.7	108.1	106.8	108.1	108.1	108.2
Prices, wages and costs											
Prices											
Harmonised CPI (% yoy)	0.9	0.8	0.4	-0.2		0.1	-0.5	-0.1	0.1	0.3	
Core HICP (% yoy)	1.1	1.2	1.1	1.0		1.2	0.9	1.1	1.0	1.1	
Harmonised PPI (% yoy)	-0.8	-0.8	-1.2	-2.0		-1.7	-2.2	-2.1	-1.7	-1.5	
Commodities, ex. Energy (% yoy)	-4.9	-1.8	0.9	2.3		0.1	2.3	1.4	3.4	0.5	
Oil price (USD)	109.7	102.0	76.4	55.1		63.1	49.7	58.9	56.8	61.6	
Inflation expectations											
EC household survey	16.9	13.4	8.6	0.5		6.2	0.5	-0.7	1.7	2.1	8.3
EC industrial survey	2.3	4.2	2.1	-0.4		-1.5	-1.2	-0.1	0.1	0.4	0.9
Unit labour cost (% yoy)											
Unit labour cost	2.0	2.0	1.8	1.8							
Compensation	2.6	2.5	2.6	2.4							
Hourly labour costs	2.4	2.1	1.7	2.5							
Money (% yoy)											
M3	4.5	4.7	4.7	7.1		4.7	5.9	6.3	7.1		
M3 trend (3m cma)						5.2	5.6	6.4			
Credit - private	-3.5	1.4	1.7	2.6		1.7	2.1	2.5	2.6		
Credit - public	9.7	5.9	12.6	32.3		12.6	19.0	15.5	32.3		

% pop = % change this period over previous period.
Sources: Deutsche Bundesbank, European Commission, Eurostat, Federal Employment Agency, German Federal Statistical Office, HWWI, ifo, Markit

Deutsche Bank
Research

Focus Germany

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