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Research Report on Germany

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Introduction

The German overall creditworthiness remains stable and sound. Germany is one of the key European players and world-leading exporter country, representing 28% of the consolidated Euro Area GDP. The constant decline of government debt indicators as well as the positive and stable fiscal balance have contributed significantly to the positive assessment of the country. However, Germany faces a number of issues which could potentially impact the country's competitiveness in the long-run. On the one hand, the recently announced monetary and trade policies at the European level could contribute positively to the external position of Germany. On the other hand, the structural issues of the country, such as aging and declining population as well as financial obstacles of German companies abroad are expected to have a negative long-term effect on the German economy.

Main Economic Indicators of Germany

Macro indicators	2012	2013	2014
Gross pub. debt, bill EUR	2174	2159	2123
Nominal GDP, bill EUR	2750	2809	2904
Real GDP growth, %	0,6	0,2	1,6
Gross gov. debt/GDP,%	79,0	76,9	73,1
Deficit (surplus)/GDP,%	0,1	0,1	0,6
Inflation rate,%	2,1	1,2	0,2
Curr. Account balance/GDP,%	5,8	5,7	6,5

Development indicators	2014
Inequality adj. HDI	0,8
GDP per capita (Thou. of USD)	45,9

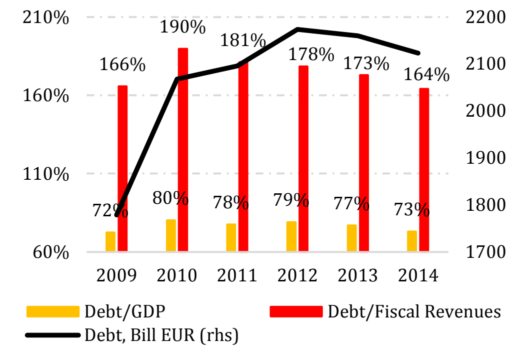
Default indicators	30.04.2015
5-Year CDS spread (Bp)	17
10Y Gov Bond Yield, %	0,28

Sources: RAEX (Europe) calculations based on data from IMF

Government debt indicators still show negative long-term trends. After reaching a peak of 2173 billion EUR in 2012, gross government debt of Germany showed a constant decline in the years which followed (see graph 1). As a result of the sharp increase of GDP and budget revenues growth rates after 2009 (see graph 2), gross government debt ratios showed a long-term negative trend since 2011. In this respect, the current debt load of Germany poses no risk to the overall creditworthiness of the country. According to IMF estimations, German GDP will grow by 1,6% and budget revenues will show an increase of 3,6% this year. In case these estimations materialize, we expect to see a further decline of debt indicators by the end of 2015.

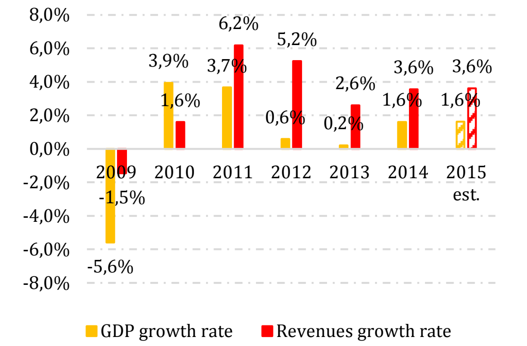
Fiscal balance of Germany still shows positive figures and is projected to remain on the same track. After the 2008 financial crisis, the German government increased its expenses significantly, which led to an enlargement of the overall fiscal budget deficit. Since 2011, the German government showed a sound fiscal stance, which still remains balanced (see graph 3). Even though IMF estimates the 2015 German fiscal surplus to decline compared to previous years, the overall balance will remain positive.

Graph 1: Trend of debt indicators



Source: RAEX (Europe) calculations based on data from the IMF

Graph 2: GDP and Budget revenues growth rates



Source: RAEX (Europe) calculations based on data from the IMF

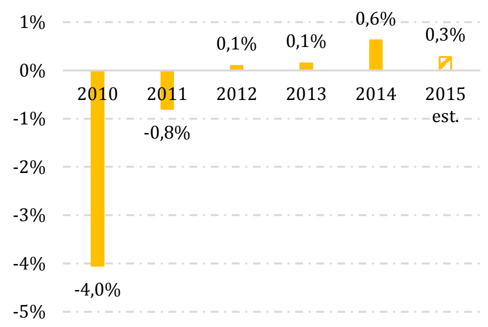
ECB's QE programme[1] and TTIP agreement[2] could compensate for loss in competitiveness caused by wage increase. As discussed in the previous research report on Germany[3], the German coalition government passed a law in 2014, which set the minimum wage at €8,5 per hour. While many analysts agreed upon the idea that a nation-wide minimum wage would eliminate the disparities in wages arising from collective wage agreements in different sectors, opponents suggested that the law would harm Germany's economic competitiveness. Even if the concerns regarding the minimum wage law were to materialize, the recently announced QE programme from the ECB as well as the proposed TTIP agreement will have a counter effect on them. On the one hand, the QE programme enforced by the ECB since January 2015 is expected to rebound inflation rate to positive ground and to increase EU's competitiveness by weakening EURO against other currencies. On the other hand, TTIP agreement shall boost competitiveness through elimination of trade tariffs between the US and the EU. Since a final agreement on TTIP has not been reached and ECB's QE programme is still in process, RAEX Europe will keep on watch further developments on these matters.

Germany's structural position remains unchanged. As discussed in our previous research report, downward long-term trend in the population of Germany has been mostly fueled by a low fertility rate[4] (1,38 in 2012) during the last decade. In addition to this, for the last 20 years the gap between the Euro area and Germany old-age dependency ratio[5] has widened suggesting that German population is ageing at a higher pace than the average European population. The shrinkage of the working-age population not only poses a potential risk for the funding of the national pension system, but also remains the key headwind to growth. With industry and trade representing 42% of GDP, Germany's export-based economy is likely to reach a crossroad if current population trends are to remain in place.

German private sector is starting to suffer from financial constraints in Russia. Shortly after the previous research report on Russia was

[1] On January 2015 the Governing Council of the European Central Bank (ECB) announced an expanded asset purchase programme (also known as quantitative easing or QE). Aimed at fulfilling the ECB's price stability mandate, this programme will see the ECB add the purchase of sovereign bonds to its existing private sector asset purchase programs.
[2] The Transatlantic Trade and Investment Partnership (TTIP) is a proposed free trade agreement between the European Union and the United States.
[3] Research report on Germany from 27th of November, 2014 (http://raexpert.eu/reports/Research_report_Germany_27.11.2014.pdf)
[4] The mean number of children that would be born alive to a woman during her lifetime if she was to pass through her childbearing years conforming to the fertility rates by age of a given year. The total fertility rate is also used to indicate the replacement level fertility; in more developed countries, a rate of 2.1 is considered to be the replacement level fertility rate.
[5] This indicator is the ratio between the total number of elderly persons of an age when they are generally economically inactive (aged 65 and over) and the number of persons of working age (from 15 to 64).

Graph 3: Fiscal balance/GDP



Source: RAEX (Europe) calculations based on data from the IMF

published last year, the German-Russian chamber of commerce unveiled the results of a poll conducted on German companies operating in Russia. In their final report, they stated that 60% of the 6 000 German companies registered in Russia directly bear the consequences of financing shortage. More precisely, 30% of the surveyed companies answered that they are suffering from financing shortage affecting their daily operations. Additionally, 36% of these companies cancelled projects in Russia or Germany, while 32% dismissed employees in some of these countries. RAEX Europe will keep on watch further developments on this matter.

Conclusion

While Germany's debt and fiscal stance remain sound and stable, there is still a number of factors which could have a negative long-term effect on the competitiveness of the country. The latest ECB's QE programme and the TTIP agreement between the EU and the US are likely to improve Germany's competitiveness abroad. In contrast, the country's overall structural position poses a risk to the funding of the national pension system and growth prospects of the country. RAEX Europe expects no significant change in the overall position of the country based on the encouraging forecasted economic conditions.