

## Market Woes Hit German Economy

September 22, 2008

BERLIN - An end to the export boom that has long underpinned German prosperity leaves the country's economy, despite its relatively sound fundamentals, facing the prospect of several quarters of low or negative growth.

As the world's largest exporter of goods, Germany is exposed to its trading partners' woes and faces a sharp slowdown in export growth. The economy is probably already in recession and shows little sign of picking up soon.

"Whatever happens to our trading partners will happen to Germany, with just a little lag," said Bank of America economist Holger Schmieding.

Citigroup economist Juergen Michels said weakening demand from both within the euro zone and beyond, combined with the lagged impact of the euro's <EUR=> recent strength, would contribute to a "likely massive slowdown in export activity".

He expected export growth of 4.7 percent in 2008 after some 8 percent in 2007, slowing further to 2 percent at most in 2009.

As Europe's biggest economy, Germany's fortunes are closely tied its neighbours'. Despite profiting from growth in emerging markets, the Middle East and eastern Europe, Germany has been unable to 'decouple' from the slowdown in big Western economies.

After growing by 1.3 percent in the first quarter, the economy contracted by 0.5 percent in the April-June period. The Finance Ministry said on Friday the third quarter likely saw another contraction, which would put Germany in recession.

Finance Minister Peer Steinbrueck this week massaged down expectations for growth next year.

"(The) severe banking crisis will cause a slowdown in economic activity," Steinbrueck told last Wednesday's edition of the Passauer Neue Presse daily, adding that 2009 growth of between 1.0 and 1.2 percent was "realistic".

The government's official forecast for German expansion in 2009 is 1.2 percent after 1.7 percent in 2008.

### "ANGLO-SAXON MISTAKES"

There is a palpable sense of frustration in Germany that the economy is being dragged down by the latest round of financial sector strife stemming from the United States, where Lehman Brothers' (LEH.N) filed for bankruptcy protection on Monday.

"We are part of the stabilising forces in this crazy development going on around us," Deputy Economy Minister Hartmut Schauerte said last Thursday. "We didn't make Anglo-Saxon mistakes. We didn't bet everything on financial services."

A strong home rental tradition in Germany has prevented a U.S.-style real estate bubble forming here, while productivity gains have helped Germany retain its position as world export leader since 2003.

The BdB private banks' association also said on Thursday there is no statistical evidence of a credit crunch in Germany. Nevertheless, the industries that have underpinned German growth are feeling the impact of other economies' weakness.

German chemicals trade group VCI on Wednesday cut its forecast for full-year sales growth for the industry to 4.5 percent from 5.5 percent previously, citing the U.S. slowdown, high oil prices and the strong euro <EUR=>.

"Chemicals companies are now starting to feel the impact of the U.S. financial crisis and the weaker dynamism in European industry," the VCI said.

Chemicals account for some 13 percent of German exports.

## CONSUMER ANGST

Germany agreed the sale last month of lender IKB (IKBG.DE), its most prominent casualty of the crisis stemming from the U.S.-subprime mortgage market. But it remains exposed to fallout from the banking crisis, which is making consumers nervous.

Germans' confidence in banks, and the overall economy, took a knock this week after state lender KfW mistakenly transferred 300 million euros to Lehman Brothers on the day the U.S. bank sought bankruptcy protection.

"Germany's stupidest bank!" ran the main front-page headline on Thursday's edition of mass-selling daily Bild. Most national newspapers ran the story on their front pages.

Consumer morale is crucial to the performance of Germany's economy as household spending accounts for over half of gross domestic product GDP.L. A drop in private consumption contributed to a 0.5 percent contraction in second-quarter GDP.

The BdB private banks' association expected Germans' savings rate to rise to by around half a percentage point to 11.2 percent of disposable income this year.

Welfare reforms have already left Germans reluctant to raise their spending despite wage gains and falling unemployment, and the banking crisis is likely to weigh on private consumption, holding back economic growth.

"We are far away from seeing any significant recovery in private consumption," said Michels at Citigroup.

# HEALY CONSULTANTS

Source: Reuters