Finanzgruppe
Deutscher Sparkassen-
und Giroverband

ECONOMIC UPDATE

Issue 2/2020

Easing measures in Europe - the virus still lurks

Berlin, 16th June 2020

Author:
Dr. Holger Schulz
Holger.Schulz@dsgv.de

In Europe, the number of new infections is declining. The Covid-19 pandemic seems to have been successfully contained. But in other regions of the world, now mainly in South America and India, the virus continues to rage unchecked. The threat remains in the world for the time being.

It will be difficult to restart the tightly interwoven global economy. In this connection, freight transport should have priority over personal transport. And it is important to keep resurgent protectionism in check. In Europe, the internal market must once again live up to its name.

The coronavirus-induced recession continues to have the characteristics of both a demand-side and a supply-side shock. The shortfall in demand is becoming increasingly important here. The predicted slump in GDP in Germany, as in Europe in general, is becoming ever deeper. Against this background, the Federal Republic’s coalition committee has launched a comprehensive economic stimulus package for Germany.

The temporary reduction in value-added tax is primarily aimed at stimulating demand as the starting point for a recovery. Many of the other measures also have a structural component and are intended to address the issues of innovation and ecology and to reduce the country’s lag on the digitalization front.

Monetary policymakers are backing up the fiscal-policy initiatives of many countries and also of the pan-European authorities by expanding their bond purchases. Money supply growth has recently accelerated significantly once again.

Easing measures in Europe - the virus still lurks

For the time being, containment has proved successful

The Covid-19 infection count has developed favourably in Germany and in most other European countries. After exponential growth in March and the peak of new infections and acute cases in April, a provisional containment scenario was achieved in May. This enabled the gradual easing of lockdown restrictions. However, it is becoming apparent that restarting a modern, highly complex economy marked by a strong division of labour will be anything but easy.

The individual products, supply and consumption channels, sectors, regions and countries are tightly interwoven. Because not all the cogs in the wheel are moving together again in step, the overall system remains at a sub-par level.

For Germany, as a country that is particularly well integrated into the global economy, the persistent problem is that in many regions of the world the trajectory of the epidemic is looking far less favourable than in Europe. The infection and death tolls are highest in the USA. Until the end of May, there were only signs of a gradual abatement of the wave there, but no breakthrough to a fundamental improvement. Daily new infection figures in the United States are still hovering at around the 20,000 mark.

The focal points of infection are to be found in the emerging markets

The trend is even more alarming in large emerging markets such as India and Brazil. In absolute terms, it is true, the number of cases in such countries is not yet as high as in the USA. But the trend there is still pointing to exponential growth. South America is becoming a hotspot of the pandemic. In Russia, the trend is not very encouraging either, although a conspicuously low death rate is being reported from Moscow.

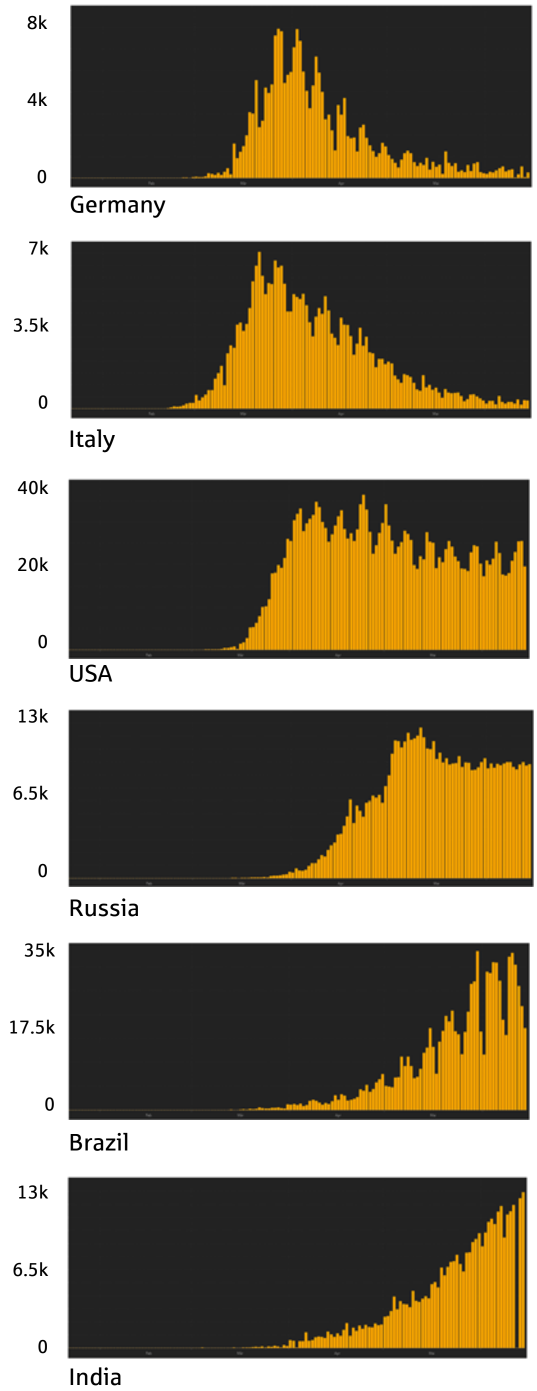
All these developments in the global environment indicate that the threat is still lurking, and will continue to do so at least until a vaccine has been found and made available to broad sections of the population.

Rules and emergency measures at the ready

Hygiene measures and vigilance remain necessary. Further opening will only be possible if numerous rules are observed. The warning system installed in Germany, which automatically calls for stricter regional rules at district level as soon as 50 cumulative new cases of infection per 100,000 inhabitants occur in a week, ensures that the necessary reaction is objective and rapid. At present, almost all Germany's districts are well below the alarm threshold, most of them even with a good safety margin. In many regions, no new cases at all have been reported in recent weeks. And yet the rule that remains indispensable indicates under what sword of Damocles we continue to operate.

It is also difficult to assess the extent to which real consumer enthusiasm can and will emerge amidst the measures that are necessary for the time being. With facemasks and social-distancing rules, some activities are not much fun. Some things simply remain unrealizable.

Daily new corona infections on an international comparison from the beginning of the year until today



Source: Johns Hopkins University, Retrieved on 15th June 2020

International movement of goods - priority for freight transport

International movement of goods will continue to be hampered for quite some time to come. This applies to the movement of both people and goods.

With the former, it is sensible and plausible – not least from an epidemiological point of view – if activity stays limited for the time being. Passenger air traffic with social-distancing rules applying in the cabin is hardly possible if airlines are to operate economically. And the reverse is also true: economic operation is not feasible if passengers are spaced too far apart.

In case of doubt, caution is advisable. After the Germans have set out again to explore a world which remains dangerous in many places, those returning from their summer holidays must not become the germ of a second wave of infections in the country.

The situation is different with the movement of goods. Here, a revival is to be hoped for at all levels and on all traffic routes. Existing restrictions and obstacles should be removed. Border controls and barriers are more than just grit in the gears. In the worst case, they can completely disrupt internationally interlinked value chains. In Europe, the "internal market" must once again live up to its name.

A gradual de-globalisation can at least be expected in any case after the current Covid-19 crisis has been overcome. The maintenance of national reserve capacities - for strategic goods (a category which will probably be much more broadly defined in future), including medical equipment or basic pharmaceutical materials - makes sense to a certain extent.

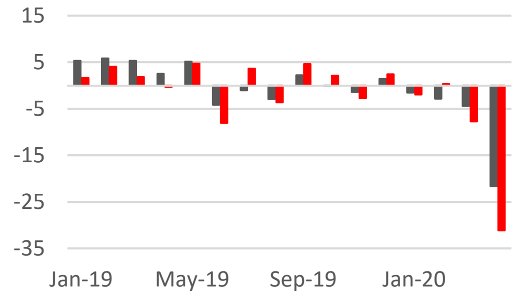
Protectionism remains a threat

On the other hand, shutting down the hatches for protectionist reasons is clearly harmful. Conflicts of that kind had already broken out before the coronavirus outbreak. And they threaten to flare up again. At the beginning of the year, at best a ceasefire was reached in the Sino-US trade dispute. The conflict could also be rekindled for political reasons (China's intervention in Hong Kong). The paradigm shift away from the multilateral world trade order, which has brought the world great prosperity for decades, was and is already in full swing anyway.

In an election year, and in the light of the divisions in American society, as currently reflected in the mass protests, the USA remains a factor of political uncertainty. What kinds of escalation threaten? What would happen if the outcome of the presidential election in November were to be a close one? What supposedly popular measures will President Trump try to mobilize in the latter stages of the election campaign? And in the Democratic camp too, decidedly protectionist instincts are a tradition.

What is new on the trade-conflict front is that "export" restrictions are now often being mentioned in many countries in connection with the coronavirus upheaval. Previously, classic trade-policy interventions, such as customs duties, almost always involved import restrictions. In the past, the aim was to channel demand for goods to privileged domestic suppliers. Now, in a new qualitative sense, it is also about the availability of key goods and intermediate products.

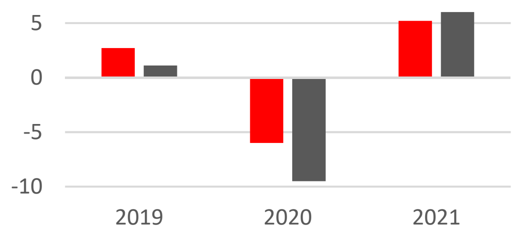
Trend in German exports and imports over time,
year-on-year change in %



Source: Federal Statistical Office

"Single Market" must live up to its name

OECD world production and trade forecasts



Source: OECD, Forecasts 2020, 2021 according to “single-hit-scenario”

The USA has also morphed into a factor of political uncertainty

Export restrictions are now becoming more frequent as well

Complex combination of supply-side and demand-side shocks

This demonstrates that the dislocations in the global economy triggered by the virus still have both a supply-side and a demand-side component. Several shocks are hitting the economy simultaneously. And, regrettably, these shocks are not offsetting each other. Unfortunately, it is not possible to cut out certain effects, thereby minimizing the overall damage. On the contrary, the supply-side and demand-side shocks are very different in their structures. The two problem groups are tending, if anything, to aggravate each other. This is what makes them so difficult to combat via economic-policy means.

Germany agreed on short-term bridging measures at an early stage. Just how beneficial the short-time working arrangements are for maintaining income flows and securing employment can be gauged from an international comparison between Germany and the USA. In the USA, unemployment immediately shot through the roof after the lockdown. May brought at least a small improvement in a countermovement, albeit at a still sharply elevated level of unemployment.

The supply-side shock persists in continuing bottlenecks in value chains and in the impossibility of goods production in certain fields. Trade fairs, major events, cultural activities and many personal services remain restricted. What is important here is to come up with specific solutions and compensations.

In the end, however, a more pronounced shift in bottlenecks to the demand side can be observed. This is reflected, for example, in the regular company surveys conducted by the IW Cologne. Companies have recently been concerned primarily about orders and sales.

This can also be seen from the orders received by manufacturing sector, which in April 2020 were 25.8 percent down on March and 36.6 percent below the April figures for the previous year. Domestic orders were hit hard, and orders from abroad even harder.

Where is the shortfall in demand originating?

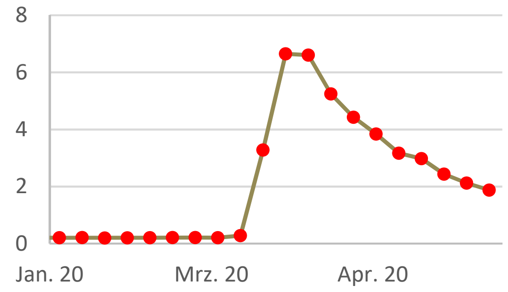
The demand-side shock has several dimensions:

The will, the trust, and the ability to buy.

One question is what and how much consumers want in the current situation. And to what extent is the prevailing uncertainty slowing down both consumption and investment? There is uncertainty about the epidemiological situation on the one hand, but also about the future economic outlook: How secure is my job? How deep and how long will the recession prove to be? What will the post-Corona world look like economically? In case of doubt, investments and the purchase of durable consumer goods will be postponed in such an uncertain situation.

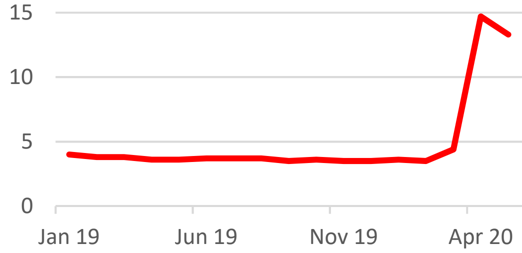
The third of the above-mentioned dimensions - economic “ability” in the sense of “What am I am able to afford?” - has to do with financial leeway. Financial resources are very unevenly distributed in the current recession. Income flows have collapsed in the case of a large number of affected people. One might think here of the many self-employed workers in the arts, in the cultural world in general, but also in the hotel and catering industry.

Initial nonfarm jobless claims in the USA,
per week in million



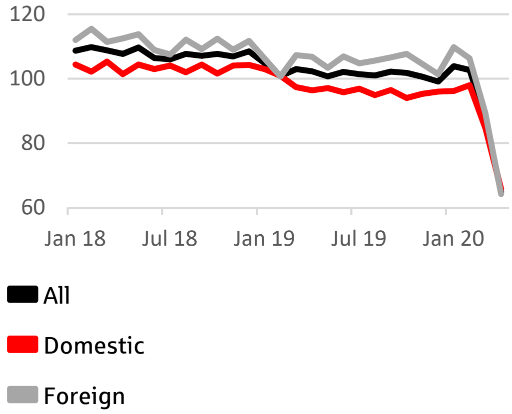
Source: U.S. Bureau of Labor Statistics

Unemployment rate in the USA, in %



Source: U.S. Bureau of Labor Statistics

New orders booked by German manufacturing industry,
indexed



Source: Federal Statistical Office

Uncertainty is putting a brake on both consumption and investment

On the other hand, income flows have been largely preserved for large swathes of the population, even unchanged in the majority of cases. Zero employment has so far been only a marginal phenomenon on the German labour market - in stark contrast to the situation in the USA, for example. However, even the majority of households with unchanged income levels have lacked many opportunities for consumption in recent weeks and months. In many cases, summer holidays and the associated expenditure are also going to be cancelled this summer. Such considerations have been reflected in the major economic stimulus package negotiated and announced by the Berlin coalition committee

Consumption opportunities are often simply not available

The savings ratio is rising...

The savings rate at private households already rose in the first quarter of 2020. In the initial estimate, the national accounts reported a seasonally-adjusted figure of 12.4 percent. In the years up to 2019, the rate was mostly stable at around eleven percent. Forecasts for 2020 as a whole predict an increase to around 15 percent. For much of 2020, German consumers will simply not be able to find spending opportunities. As savings banks, we too are observing this development as many current accounts are overflowing with spare cash.

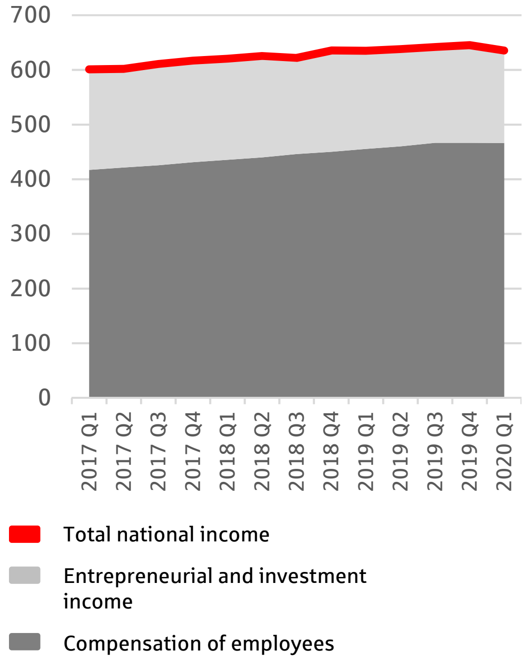
Forecasts of the savings ratio in Germany
(share of income of private households in %)

Institute	Date	2020	2021
BMWi	May 20	15.5	10.5
ifo	Apr 20	15.0	11.0
IMK	Apr 20	11.4	11.0
Joint diagnosis	Apr 20	15.0	11.0
IfW	Mar 20	11.6	-

... with wage income remaining very stable

The slump in production and national income during the acute phase of the crisis is now reflected in the first estimate for the first-quarter national accounts data. According to this, the losses triggered by the shutdown had to be borne almost entirely by entrepreneurial and investment income. By contrast, total compensation of employees actually continued to rise until the first quarter of 2020, regardless of whether the development is compared to the same quarter of the previous year or, in seasonally-adjusted terms, to the final quarter of 2019.

Composition of German national income



All in billion euros per quarter, seasonally adjusted

Source: Federal Statistical Office

The divergence between income types is not a new development seen only since the outbreak of the Covid-19 epidemic, but has been observed for some time. The trend was already inherent in the weak productivity figures and in the "industrial recession" evident since mid-2018. Employment and wages rose even further in 2019, but with the overall economy stagnating, not from a larger overall cake, but increasingly at the expense of earnings on profit. This development has now continued and become more exacerbated during the coronavirus crisis.

In principle, this trend in functional income distribution is good for the protection of lower income groups and for maintaining purchasing power during a recession, as long as corporate profit margins still allow this without a company's existence being endangered. Unfortunately, the latter must be doubted in the present acute crisis in the most affected industries, as the increasing numbers of company bailouts which are becoming necessary show.

As already mentioned: among wage earners too, there are many cases of people who are directly and strongly negatively affected where this is different: But regarding "mass incomes" as a whole (defined as the sum of wage and transfer incomes) "money" is not the problem. Sufficient general purchasing power would be available.

Low incomes entailing a high consumption ratio are looking relatively stable

What is important, then, is to get households back on the consumption track - by building confidence and providing price incentives.

Economic stimulus package worth EUR 130 billion announced

The guarantee that social security contributions in 2020 and 2021 will not rise above the 40 percent mark is intended to build confidence and ensure that companies and private households can plan ahead. Deficits in the social-insurance budget would be compensated for by the federal government.

Selected elements of the "Economic Stimulus and Crisis Management Package" of the Coalition Committee dated 3rd June 2020

- **Temporary reduction of the VAT rate**
  - From 1st July 2020 to 31st December 2020 the VAT rate is to be reduced from 19 % to 16 %.
  - The reduced rate is to be decreased from 7 % to 5 %.
  - **Financial requirements:** 20 billion euros

- **Social guarantee 2021:**
  - Stabilisation of social security contributions at a maximum of 40%.
  - **Financial requirements:** EUR 5.3 billion in 2020, requirements in 2021 can only be determined in the context of the 2021 budget statement

- **Gradual reduction of the Renewable Energies levy:**
  - From 2021, the Renewable Energies levy is to be reduced through subsidies from the federal budget
  - Planned electricity prices: 2021 at 6.5 ct/kwh and 2022 at 6.0 ct/kwh
  - **Financial requirements:** 11 billion euros

- **Increased tax loss carryback possible**
  - For the years 2020 and 2021, the loss carry-back is to be extended to a maximum of EUR 5 million and EUR 10 million (in the case of joint assessment for married couples)
  - A mechanism will be introduced to allow the loss carryback to be used in the 2019 tax return
  - **Financial impact**: shifting effect 2 billion euros, of which 1 billion euros federal government

- **Short-time benefits:**
  - From 1 January 2021, a reliable scheme for the payment of short-time working allowances will be presented

- **To strengthen the municipalities**
  - The federal government will permanently cover a further 25% and a total of 75% of the costs of accommodation and heating for the needy in the existing system
  - In addition, the federal government should strengthen local public transport and the health sector of the municipalities
  - **Financial requirements**: 4 billion euros per year

- **Municipal solidarity package 2020**
  - With this package, the current crisis-related shortfall in trade tax revenue will be half financed by the federal government
  - In the case of trade tax, an allowance for the existing addition facts is increased to 200,000 euros
  - **Financial requirements**: 5.9 billion Euro Federal Government

Such an approach is meaningful and expedient because the deficits in the social security system are partly due to the closures and hygiene measures ordered by the government. The budget of Germany's Federal Employment Agency is being burdened by the one-time special situation. This should not be offset by increasing contribution rates.

Capping social security contributions will maintain their function as an automatic stabilizer

Only if rates remain constant can the social security systems play their role as automatic stabilizers.

The reduction in VAT is the first element mentioned in the Coalition Committee's paper, and is also the most prominent and currently most widely discussed aspect. The funding needed to bring down the general tax rate from 19 to 16 percent and the privileged rate from 7 to 5 percent for six months alone is estimated to amount to 20 billion euros.

The cut in VAT will have mixed effects, being only partially handed on to final consumers

The question of the extent to which the tax reduction will show up in retail prices or whether it will end up in full in retailers' coffers is being keenly discussed. In practice, the effects will probably be mixed. It will depend on the market situation in each individual industry, the cost situation, the extent to which the company is being affected by the crisis and, in particular, the intensity of competition. In this respect, a free market economy can be trusted to have a certain ability to organise itself.

The VAT reduction is likely to be passed on in part - both effects will work

And both effects would, in their own ways, have beneficial consequences. Already in the case of the temporary tax reduction for the catering trade which is already in force, the aim is, in a supply-side manner, to stabilise net sales in an industry which has been particularly hard hit by the shutdown and by the restrictions still in force. If something were to "trickle down" here to strengthen the companies, that would not be a bad thing at all. This is also the point of departure in many other sectors.

In other sectors again, the hoped-for effect is additional consumption due to a passed-on price incentive. That works best with consumer durables, where, at the very least, a tax change can trigger an anticipatory effect.

On the other hand, the empirical results of such cyclically motivated VAT cuts are rather sobering. A look at the experiences in other countries reveals the following. In its more than a decade mired in stagnation and deflation, Japan increased its sales tax, introduced in 2006, in several stages. Great Britain temporarily reduced its VAT during the financial crisis. Yet effective additional consumption generated through lower VAT rates was mostly modest. Additional consumption was most likely to accumulate at the end of a phase of temporary tax cuts as an anticipatory effect before the cliff effect of a renewed tax hike. One could indeed almost argue that the announcement of the renewed tax hike was a more effective instrument than the actual reduction.

Limiting the reduction phase is the decisive element

This insight has been implemented with undeniable wisdom in the new German economic stimulus package. Narrowing down the time scale for the reduction phase to the second half of 2020 was intentional and is correct.

On the one hand, this limits the fiscal costs of such a measure. On the other hand, the achievable effects are bundled in a targeted manner. The announcement that the VAT rate is to be raised again is, in effect, the real incentive.

This is why the proposals doing the rounds to possibly extend the reduction phase are misguided, and why such a debate is even detrimental to the effectiveness of the measure.

Admittedly, it will primarily be anticipatory effects that can be achieved by the temporary reduction in VAT. However, if the timing is right, this may well prove thoroughly sensible and helpful. By definition, "stimulus packages" are always "flashes in the pan". But in extreme situations like the present one they are necessary to keep the embers alive at all. Now it is a matter of overcoming the paralysis of consumers and their reluctance to buy. In the second half of 2020, this stimulus may well become the initial spark for a general recovery and revival.

The timing of a tax-induced purchase incentive is decisive

"Crisis Management and Future Package"

Most of the other measures in the package complement the short-term stimulus with distributional-policy factors and structural components. It is therefore right that the package has a broader name. Conceptually, it goes beyond a purely cyclical effect. But if so much money is going to be disbursed, it is good to use it to also engender qualitative improvements.

It is also right to focus on innovation, an ecological orientation and eliminating digitization deficits. It is also good that "conservation-oriented" funding that would have stood in the way of these objectives was dispensed with.

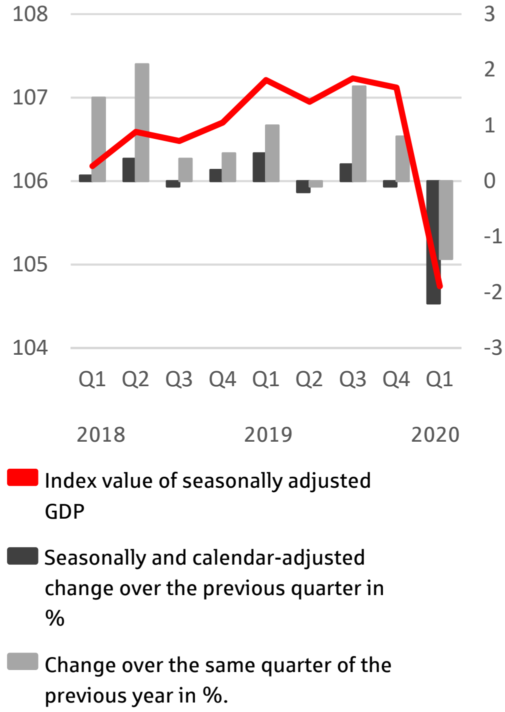
European Reconstruction Fund

Similar qualitative advances as in the German package are also outlined in the European Reconstruction Fund which is under discussion. According to the proposals, 500 billion euros is to flow in the form of grants, with an additional 250 billion euros becoming available as loans. An important component in the project, which still has to surmount difficult political hurdles, is the redistribution between nations that goes hand in hand with it. This is an important obstacle to acceptance for the net donor countries. But without such a redistributional component, the project would not need to be located at the European level at all. Ultimately, it is in the donor countries' own interest if such a piece of architecture preserves the domestic market and shores up ailing sales markets.

The EU should not misuse the crisis to engineer shifts in sovereignty

It is important, however, to ensure that only this concrete crisis and crisis-containment benefits are at stake, and that budgets and sovereignty are not permanently established at a European level as an end in itself. Liability rules and competences must not be blurred and shifted. This remains the central task on the agenda for the German Council Presidency in the second half of 2020, not least in view of the mounting pile of zone-wide debt.

Quarterly development of German GDP



Source: Federal Statistical Office

Q1 national accounts only capture the beginning of the shutdown

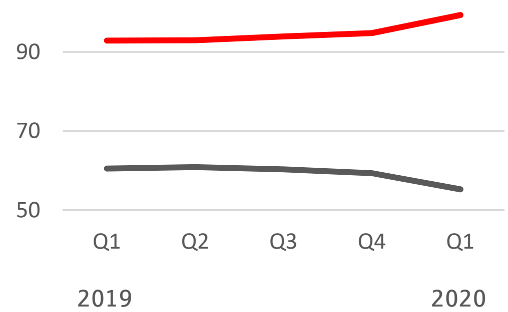
The extent of the recession suggests that the recovery needs to be actively accompanied by fiscal measures at a European and national level in the aftermath of the current deep slump in economic activity. So far, only the first quarter national-accounts data is available. This only covers the initial phase of the shutdown, which came into force in Germany in mid-March. This does at least mean that two weeks of actual figures have been included in the data set for the first time.

Over the first quarter as a whole, gross domestic product contracted by 2.2 percent in real, seasonally-adjusted terms compared to the previous quarter. This is the biggest setback since the financial crisis a good ten years ago. And Q2 GDP is already expected to slump even more sharply because the second quarter contained a larger share of the shutdown phase. As expected, in the first quarter both private consumption (-3.2 per cent relative to the previous quarter), investment in equipment (-6.9 per cent) and exports (-3.1 per cent) were responsible for the decline in GDP. Government consumption already stabilised slightly in the first quarter (+0.2 per cent). Construction investment likewise had a positive effect (+4.1 per cent), benefiting from the mild winter in January and February. And construction is one of the few sectors that were also largely spared from a shutdown perspective. But of course, construction activity alone cannot function as a central pillar of GDP.

Concerning the trajectory for the rest of the year, it is obvious by now that the second quarter has already been largely "lost." In the wake of this, hopes are now being pinned on an overall economic recovery in the second half of 2020 and then in 2021, on the back of the lockdown-easing measures.

Development of equipment and construction investment in Germany

Seasonally and calendar-adjusted, in billion euros



Source: Federal Statistical Office

Forecasts for 2020 as a whole have settled to some extent

We can presumably no longer count on the originally touted scenario, a rapid "V-shaped" recovery. Expressed in the graphic "letters" which have become customary, the path will probably be either a "U", which is now the best-case scenario, or else an "L", which would see GDP languishing at a low level for a long time. A "W" is also possible if there are economic setbacks or, in the worst case, new waves of epidemiological setbacks when the economy is reopened.

While the annual forecasts were revised in a very wild and volatile manner in March and April, when the full extent of the shutdown was first becoming clear, resulting in a veritable "race to the bottom", the forecasts of most relevant institutions largely came back into line in May. The scatter of forecasts is still a broad one, which is not surprising in the extraordinary situation. However, the scatterplot has remained largely stationary in recent weeks in the range of -5 to -10 percent.

GDP forecasts for Germany 2020 and 2021,

real, in %

GDP forecast	Date	2020	2021
Bundesbank	Jun 20	-6.8	3.2
Deka	Jun 20	-7.3	7.5
DIW	Jun 20	-9.4	3.0
ifo	May 20	-6.6	10.2
EU Commission	May 20	-6.5	5.9
IWF	Apr 20	-7.0	5.2
OECD single-hit-sc.	Jun 20	-6.6	5.8
OECD double-hit-sc.	Jun 20	-8.8	1.7

The OECD has sub-divided its recently published early summer forecast into two scenarios, depending on whether the world is spared a second wave of infections or whether those countries that have already succeeded in containing the number of cases are hit even harder a second time. This divergence would make a difference, especially for the European economies. For Germany, the OECD projects -6.6 and -8.8 percent as GDP forecasts for 2020 under the two scenarios. Both figures fit largely into the, in any case, broad field of current forecasts.

For 2021, the difference in the OECD recovery rate is even more pronounced: 5.8 percent GDP growth under the "single-hit" scenario, but only 1.7 percent under the "double-hit" scenario. Although the hypothetical second wave is located before the end of 2020, it would have correspondingly negative effects in 2021, because the baseline would remain depressed for longer and the start of the recovery would shift later into the coming year.

The strength of the recovery will make the difference

In general, the forecasts of the other institutions for 2021 and the subsequent period also diverge rather markedly. Almost everywhere, a fairly strong recovery is the main scenario. But the forecasts differ considerably in the degree of optimism as to whether the old pre-crisis level can soon be reached again - or in some particularly confident cases even exceeded. A case in point is the forecast of the ifo Institute, which in spring very early on published very gloomy scenarios of a slump in the present year, but which now holds out the prospect of a very strong recovery for 2021.

Inflation dynamics remain weak - the ECB increases its purchases

The upward pressure on prices remains significant in the current phase. Energy and raw material prices are under pressure due to lower economic activity, as supply coming out of producing facilities is generally inelastic in the short term. However, downward price pressure can also be observed at the final consumer level for many goods. For example, the textile retail trade is currently trying to sell off its brimming inventories. During the shutdown, practically a complete collection lay around idle in warehouses.

According to the first estimate for June, consumer prices in the euro area inched up at an annual rate of only 0.1 percent in the euro area and 0.2 percent in Germany (HICP). The subdued pace of inflation was mainly due to energy prices. Core inflation rates are looking more stable at around one percent. Yet the price indices are currently being compiled with a high degree of uncertainty: many prices must still be estimated due to suspensions of actual activity.

Despite the current downward pressure, it remains open in the medium term what will happen to price developments. The impact on productivity, more expensive hygiene requirements and the significant pressure on profit margins could sooner or later force companies in many sectors to raise prices. Food products are already showing upside pricing pressure.

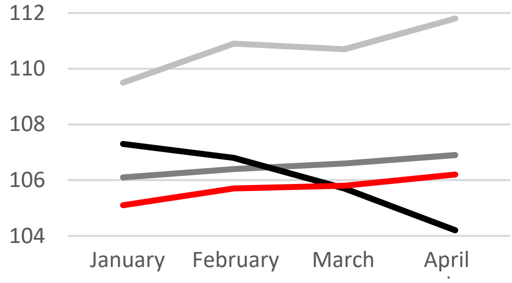
In this inflationary and economic situation, the European Central Bank has reacted once again by making its policy stance more accommodative still. This step was based on the new ECB staff macroeconomic projections prepared for the Governing Council meeting on 4 June. According to the main scenario in the economic growth projection, the euro area economy is expected to shrink by 8.7 percent in the current year. In 2021, the ECB expects a strong recovery of 5.2 percent. However, euro area GDP is not expected to get back up to its pre-crisis level again until 2022.

At the euro area level, too, inflation looks fated to remain similarly depressed. The ECB's inflation projections assume an increase in the HICP of only 0.3 percent in 2020, which is then expected to rise by 0.8 per cent in 2021. However, the ECB believes that long-term inflation expectations are still reasonably well anchored at the target level. The effect of the newly announced temporary German VAT reduction has not yet been factored into the forecast inflation rates. As the most important member of the euro area, Germany is also likely to have an impact on the overall euro area HICP, pushing it down further over the remaining course of 2020. On the other hand, the reversion to the higher tax level in 2021 will help the turnaround in the inflation rate.

In response to the sharp current slump, the ECB has once again increased the degree of accommodation in what was already a very expansionary monetary-policy stance. It has chosen the "Pandemic Emergency Purchase Programme" (PEPP), which was only introduced in the spring, as an instrument for this purpose. The PEPP's firepower is now to be increased from EUR 750 billion to EUR 1,350 billion. And the horizon for net purchases under the PEPP is to be extended from the end of 2020, the previous target, to mid 2021.

The ECB intends to purchase bonds flexibly during this period. Only on an aggregate basis will the PEPP take its bearings by the ECB's capital key.

Selected sub-components of overall inflation in Germany

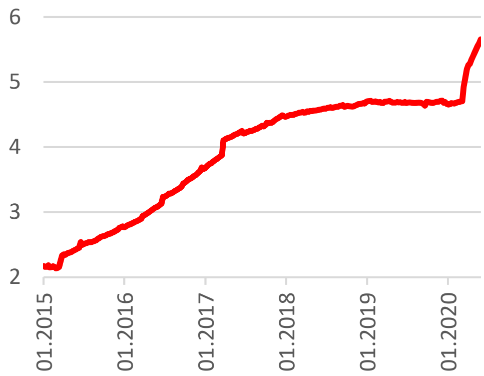


Index levels 2020; Base year 2015

Source: Federal Statistical Office

Consolidated balance sheet total of the Eurosystem,

in 1,000 bln. Eur.



Source: ECB

One factor proving beneficial here is that the supply shortage for Bunds is being alleviated by the expansionary fiscal stance being adopted in the Federal Republic. In keeping with the ECB's capital key, around a quarter of the PEPP, which has now been increased by EUR 600 billion, is roughly equivalent in volume to the German economic stimulus package.

The monetary expansion is accelerating

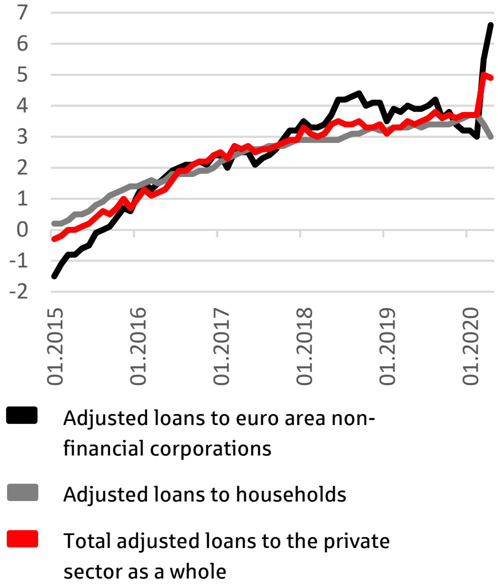
In view of monetary developments, there is no need for the ECB to accelerate further. This is because money-supply growth, which has not been weak in recent years, has recently speeded up very sharply. This reflects the strong increase in lending during the crisis, for example in the form of the numerous bridging and support loans.

During the crisis, lending dynamics in the euro area have shifted from loans to private households to corporate loans.

In April, the broad monetary aggregate M3 in the euro area grew at an annual rate of 8.3 per cent. M1 even increased by 11.9 percent. This shows that the monetary expansion is credit-driven on the one hand, but that, on the other hand, on the liabilities side of bank balance sheets, it is mainly taking place in the brimming-over current accounts of private households. The growth of the monetary aggregates also means, however, that credit financing is working well and that the stimulus desired by monetary policymakers is arriving in the real economy. From the vantage point of the banking system, there is nothing standing in the way of a renewed upswing in the post-Corona era.

Trend in various credit types in the euro area

Year-on-year change in %, seasonally adjusted



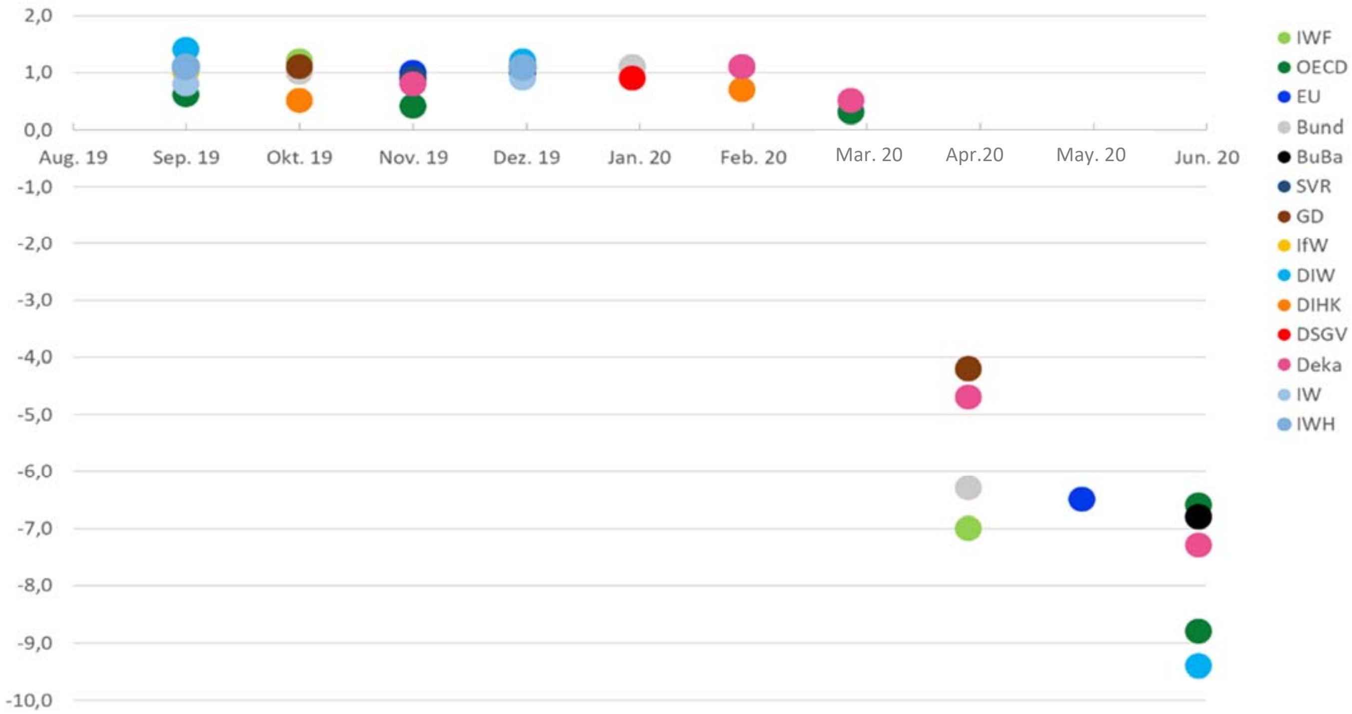
Source: ECB

A. Growth of the world economic regions, change from previous year

	2018	2019	2020*	2021*
World trade volume	3.7%	1.0%	-11.0%	8.4%
GDP - World	3.6%	2.9%	-3.0%	5.8%
USA	2.9%	2.3%	-5.9%	4.7%
Japan	0.3%	0.7%	-5.2%	3.0%
China	6.6%	6.1%	1.2%	9.2%
EU	2.1%	1.7%	-7.1%	4.8%
Euro area	1.9%	1.2%	-7.5%	4.7%
Germany	1.5%	0.6%	-7.0%	5.2%

* Forecast from the International Monetary Fund April 2020

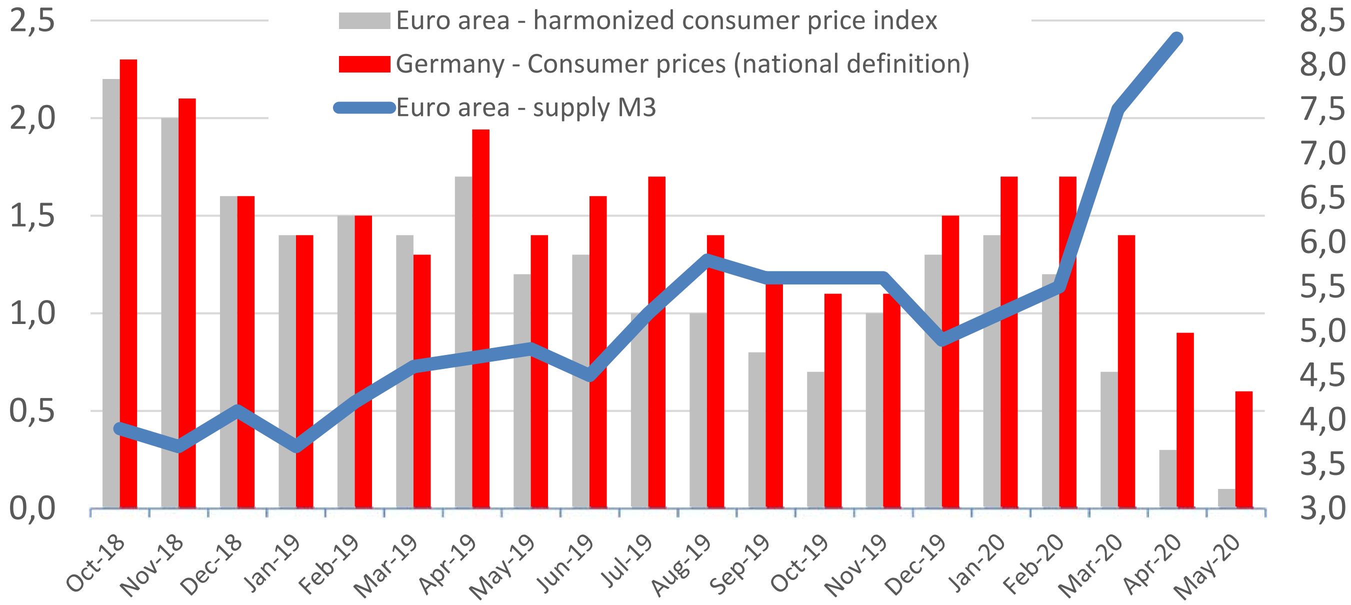
B. Forecasts for economic growth in Germany for 2020, in %



C. GDP in the Euro area and Germany

	Year 2019	Q II - 2019	Q III - 2019	Q IV - 2019	Q I - 2020
	real vs. previous year	real change compared to the same quarter of the previous year and seasonally-adjusted real change from the previous quarter			
Euro area GDP	+1.3%	+1.2% +0.1%	+1.3% +0.3%	+1.0% +0.1%	-3.1% -3.6%
Germany GDP	+0.6%	-0.1% -0.2%	+1.2% +0.3%	+0.2% -0.1%	-1.9% -2.2%
Private consumption	+1.6%	+1.8% +0.2%	+2.3% +0.2%	+1.2% 0.0%	-2.2% -3.2%
Gross fixed capital formation	+2.6%	+2.2% -0.3%	+3.2% -0.1%	+0.4% -0.4%	-0.2% -0.2%
Exports	+0.9%	-1.3% -1.4%	+2.7% +1.3%	+0.8% -0.6%	-3.2% -3.1%
		Level, not change rate, quarterly figures seasonally adjusted			
Savings rate	10.9%	10.7%	10.9%	11.1%	12.4%

D. Consumer prices (left-hand scale) and money supply M3 (right-hand scale), annual rates of change in %



E. Monthly economic indicators Germany

	Jan 20	Feb 20	Mar 20	Apr 20	May 20
Prices (nat. definition)			Change to previous year		
Consumer prices	+1.6%	+1.7%	+1.4%	+0.9%	+0.6%
- without food and energy (core rate)	+1.5%	+1.5%	+1.3%	+1.2%	-
Producer prices for commercial products	+0.2%	-0.1%	-0.8%	-1.9%	-
Import prices	-0.9%	-2.0%	-5.5%	-7.4%	-
Sentiment indicators					
ifo-Business-Climate Index	95.9	96.0	86.0	74.2	79.5
ZEW- Economic Expectations	26.7	8.7	-49.5	28.2	51.0
Incoming orders			Change compared to previous year		
Manufacturing industry	-1.9%	+0.7%	-11.9%	-36.7%	-
from within the country	-7.7%	-4.0%	-9.3%	-32.0%	-
from abroad	+2.4%	+4.3%	-13.7%	-39.8%	-
Producers of capital goods	-2.9%	-0.3%	-21.7%	-47.2%	-
Production			Working day adjusted change compared to previous year		
Producing sector as a whole	-1.5%	-1.8%	-11.3%	-25.3%	-
thereof construction	+15.0%	+4.5%	+4.4%	+0.9%	-
thereof industry	-3.0%	-2.6%	-14.0%	-31.2%	-
Foreign trade			Change compared to previous year		
Exports	-1.9%	+0.3%	-7.7%	-31.1%	-
Imports	-1.5%	-2.8%	-4.4%	-21.6%	-
Labour market			Jobless rate/change in jobless total vs. the same month of the previous year in 1000		
Unemployment rate	4.9%	5.3%	5.1%	5.8%	6.1%
Unemployed	+20	+23	+34	+415	+577
Employed persons (with place of work in Germany)	+199	+160	+82	-218	-
Employees subject to social security contributions	+434	+394	+330	-	-

F Commodity, foreign exchange and financial markets

	Feb 20	Mar 20	Apr 20	May 20	12.6.2020
Brent oil price in US $	50.5	22.7	25.3	35.3	41.7 (10.)
Exchange rates					
US- Dollar / EUR	1.0905	1.1063	1.0862	1.0902	1.1348 (11.)
Japanese Yen / EUR	120.03	118.9	116.97	116.87	121.52 (11.)
Stock Markets					
German share index DAX, end of month	11,890.35	9,935.84	10,861.64	11,586.85	12,072
Change compared to previous year	+3.25%	-13.8%	-12.01%	-1.2%	-
Money and capital market interest rates					
call money (EONIA)	-0.45%	-0.45%	-0.45%	-0.46%	-0.46% (11.)
1- Monthly deposit (EURIBOR)	-0.47%	-0.48%	-0.43%	-0.46%	-0.48% (11.)
3-monthly money (EURIBOR)	-0.41%	-0.42%	-0.25%	-0.27%	-0.36% (11.)
Current yield on German government bonds with a residual maturity of ten years	-0.61%	-0.47%	-0.50%	-0.41%	-0.40%
Interest rates of credit institutions, new business					
Overnight deposits of households, in Ger.	0.00%	0.00%	0.00%*	-	-
for comparison in the euro area	0.02%	0.02%	0.02%*	-	-
Deposits of households up to 1 year in Ger.	0.15%	0.12%	0.14%*	-	-
for comparison across the euro area	0.33%	0.31%	0.22%*	-	-
Corporate loans up to € 1 million ov. 5 y. in Ger.	1.47%	1.47%	1.76%*	-	-
For comparison across the euro area	1.48%	1.59%	1.69%*	-	-

* provisional figure

Imprint

Publisher
German Savings Banks and Giro Association
Department of Economics, Financial Markets and Economic Policy

Charlottenstrasse 47
10117 Berlin
Phone: 030 20225-5303
DSGV-Volkswirtschaft@DSGV.de
www.DSGV.de/en

Editorial deadline
15th of June 2020

Design
Franz Metz, Berlin
Photo credits
Title page: Plainpicture/Westend61

ISSN
2509-3835

Responsible
Pia Jankowski – DSGV
Head of Department Economics, Financial Markets and Economic Policy
Pia.Jankowski@dsgv.de

Dr. Reinhold Rickes - DSGV
Head of Economics
Reinhold.Rickes@dsgv.de

Author
Dr. Holger Schulz
Holger.Schulz@dsgv.de

Note
All publications in this series can be found at
https://www.dsgv.de/en