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Economic Research

Economic Briefing

Germany – Ifo keeps falling

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Dr. Ralph Solveen

The Ifo business climate deteriorated further in August, falling from 87.0 to 86.6. Companies are increasingly giving up their hopes of an economic upturn. On the contrary, they now realize that the economy has weakened as of late. This does not bode well for the German economy in the coming months.

More bad news for the German economy: the Ifo business climate fell from 87.0 to 86.6 in August, continuing the downward trend that began in the spring. This means that the indicator's increase in the first few months of this year has proved to be a false signal. A recovery of the German economy in the coming months is becoming increasingly unlikely.

A look at the sub-components shows that the decline in August is primarily due to an (even) worse assessment of the current situation. However, expectations have also deteriorated further, having already fallen significantly in recent months. They are now only slightly more positive than at the start of the year (Chart 1). While there have been ups and downs in expectations over the past two years, the assessment of the situation has shown a clear downward trend for almost three years.



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Chart 1 - Ifo: Expectations of firms disappointed again

Subcomponents of the Ifo business climate for Germany, 2015=100

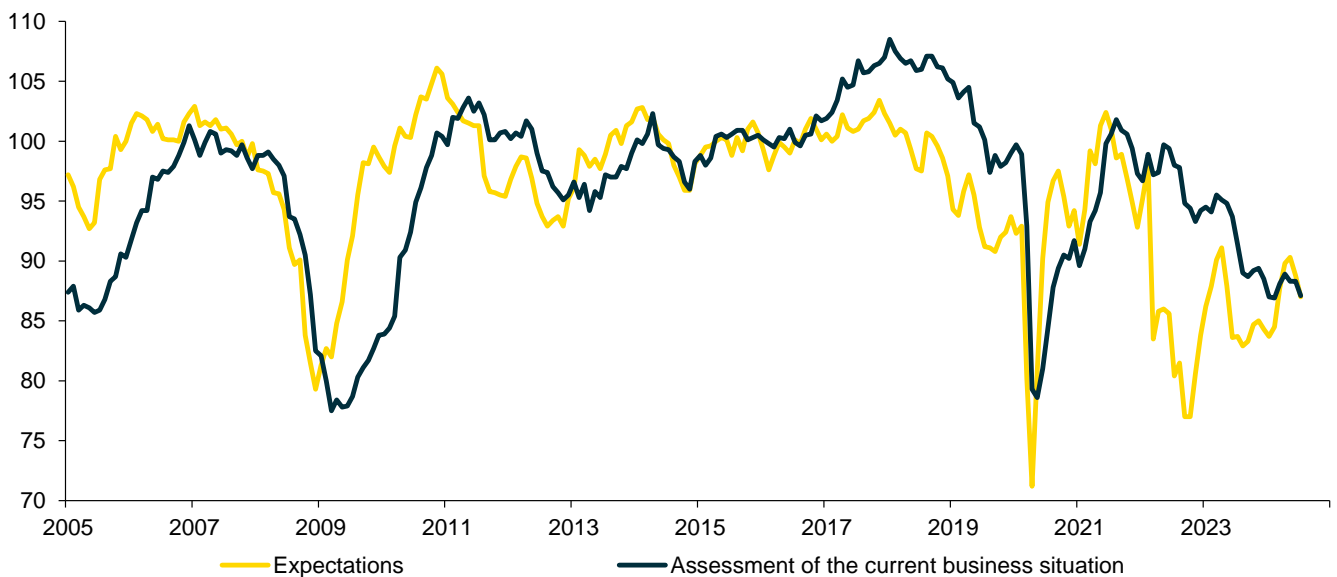


Source: Ifo, S&P Global, Commerzbank Research

Such a development is very unusual. One of the strengths of the Ifo Business Climate as a leading indicator for the German economy is that it relies on the expectations and thus the “gut feeling” of the respondents. The Ifo Business Climate therefore typically indicates turning points earlier than surveys that only look at the current situation. For example, Ifo business expectations were often well ahead of the assessment of the current situation in previous cycles (Chart 2).

Chart 2 - Ifo: Expectations have normally preceded the assessment of the current business situation

Subcomponents of the Ifo business climate, 2015=100



Source: Ifo, S&P Global, Commerzbank Research

In the past two years, however, companies’ expectations that the economy would pick up again were disappointed. The upward trend in expectations at the turn of 2022/23 may have been due to the fact that many companies – as well as the majority of analysts



- underestimated the effect of the ECB's massive interest rate hikes and placed too much faith in the relief following lower energy prices. The current renewed disappointment among companies is more difficult to explain. The adjustment to the higher interest rate level may take longer than expected and the uncertainty among consumers seems to be lasting longer. Added to this are the numerous structural problems in the German economy, which are slowing down the underlying momentum of the economy. This unfavorable combination of factors suggests that the German economy will barely grow in the second half of this year and will at best stagnate for the year as a whole. Most growth forecasts for the coming year are still likely to be too high. We expect a meagre increase of 0.5% for 2025.



Analysts

Dr. Ralph Solveen

Senior Economist

+49 69 9353 45622

ralph.solveen@commerzbank.com

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Commerzbank Offices

Frankfurt

Commerzbank AG
DLZ - Gebäude 2,
Händlerhaus
Mainzer Landstraße 153
60327 Frankfurt
Tel: + 49 69 136 21200

London

Commerzbank AG
PO BOX 52715
30 Gresham Street
London, EC2P 2XY
Tel: + 44 207 623 8000

New York

Commerz Markets LLC
225 Liberty Street, 32nd
floor,
New York,
NY 10281-1050
Tel: + 1 212 703 4000

Singapore

Commerzbank AG
128 Beach Road
#17-01 Guoco Midtown
Singapore 189773
Tel: +65 631 10000