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# Germany: Leader To Laggard

Disrupted global trade is weighing on Germany's performance.



The eurozone economy bounced back from a winter recession in the second quarter, with real gross domestic product (GDP) growing 0.3% quarter over quarter. But the headline number masks **weakness** in major economies, particularly in Germany.

After a decade of robust economic performance, Germany entered the pandemic with poor momentum and has struggled to regain its stride. The German economy was among the last in Europe to return to pre-COVID output levels. Germany is the only nation among the world's

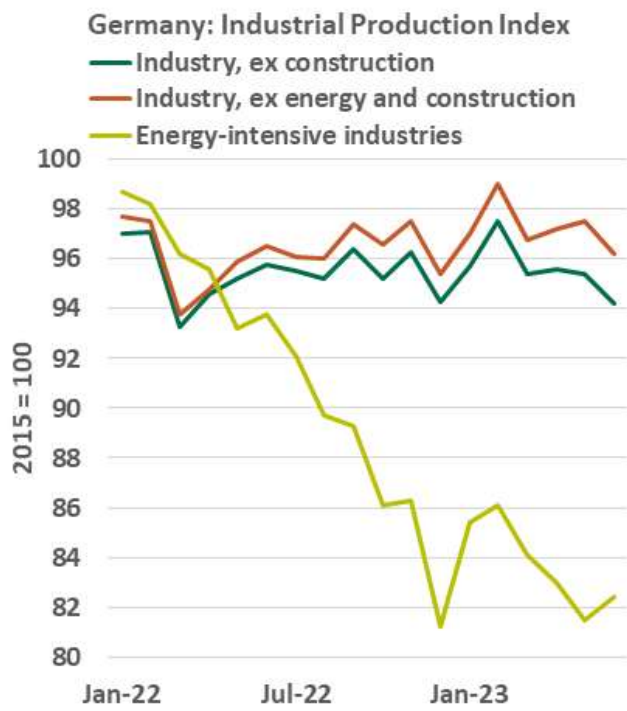
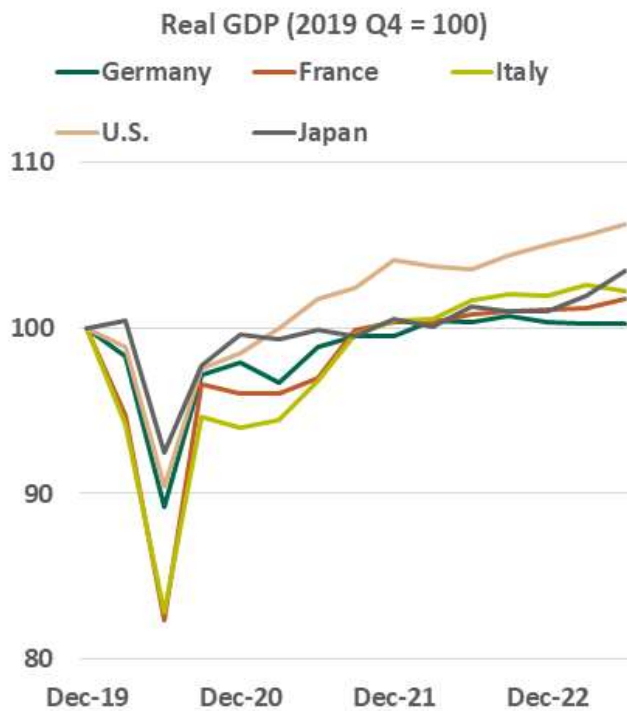
seven most advanced economies (G7) that slipped into recession at the start of the year. Going by the Bundesbank's estimates, the picture isn't going to change in the third quarter. In fact, the International Monetary Fund predicts Germany will be the only G7 economy to contract in 2023.

The current economic stagnation is drawing comparisons with the troubles of the late 1990s, when the nation was dubbed "the sick man of Europe." Deutschland may be falling ill again, but its challenges are very different today. Stubborn unemployment was one the major problems facing the economy in the aftermath of unification. Today, jobs are plentiful, with companies facing labor shortages. The German jobless rate stands at 3.0%, well below the eurozone's 6.4%.

Germany is struggling because its industries are faltering. The local Purchasing Managers' Index for manufacturing is languishing below 40 (any reading under 50 indicates contraction). Production in energy-intensive factories is down 17% since the start of last year. Automobiles have been Germany's main export for some time, but even that sector is struggling amid stiff competition from China. All of this does not bode well for an economy where manufacturing contributes about one-fifth of GDP, almost double the percentage seen in the U.S., the U.K. and France.

The disruption caused by the Ukraine war, higher interest rates and supply chain realignment are all hampering German industries. The country's export-oriented growth model is facing challenges not just from rising geopolitical strife, but also from a slowdown in its largest trading partner, [China](#).

Energy prices are not in crisis anymore, but elevated gas and electricity costs are still a factor. Germany is one of the most energy-efficient countries in the continent but the *Energiewende* (or green transition) could prove to be painful for an economy which uses nearly twice as much energy as the second largest consumer in Europe.



Sources: Haver Analytics, Destatis

The German state and industries not only appear to be ill-prepared for the energy challenge, but some misguided policies are in place. With inexpensive Russian gas no longer an option, sunsetting nuclear power could prove to be a costly decision. Power grids are suffering from a lack of **investment** that could make them more efficient.

Hopes that services will underpin the economy are vanishing, with the sector set to join the recession in manufacturing. Higher inflation remains a source of pain for consumers. Rising interest rates are weighing on activities like construction, which rely heavily on borrowing. Not so long ago, Germany was the prime mover of the eurozone economy, accounting for almost 30% of the currency union's output. The former juggernaut is now dragging the entire bloc down.

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