

Will Germany's Slowdown Doom Global Growth?

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by Roya Wolverson

As if Europe doesn't already have it bad enough, here comes some more foul news: Germany's growth, widely considered to be the saving grace of the flailing eurozone, is grinding to a halt. The question is what that means for struggling Europe and the global recovery.

Only a year ago, the region's biggest economy seemed to be powering full-steam ahead. This buoyed the spirits of global investors, even though troublesome Greece was crumbling. That's because back then, most of us assumed that even if Greece imploded, at least healthier economies like Germany and France would keep greater Europe plugging along. Granted, a lot of European countries, including France, complained about Germany's growth, since its industries benefited from lower-wage labor than elsewhere in Europe and a weak euro that make German exports cheaper. But then, at least something on the continent was going right and keeping the euro intact. Now the eurozone crisis is much, much bigger, and the challenges ahead – the potential collapse of Italy and Spain – will take even more ammo from richer Germany to fully address.

(MORE: [What the New Greek Deal Means for the U.S.](#))

Therein lies the problem. The latest slowdown in Germany – its economic growth rose by a mere 0.1% in this year's second quarter – looks like a big fat sign of foreboding, not just for Europe, but for the global economy. Slow German growth could make the edgy Germans even more opposed to chipping in for eurozone economies in distress. And tighter German finances could make bondholders more skeptical of risky Italian and Spanish debt, prompting higher borrowing costs for those countries and slower even European growth. As Ralph Atkins notes [in the *Financial Times*](#):

It is hard to see any dramatic reacceleration in Germany or the eurozone. Eurozone exports are already stalling – falling by almost 5 per cent in June compared with May, according to separate seasonally adjusted data on Tuesday. In July, German and EU exports to China were down 11 per cent compared with the second-quarter average, calculates Barclays Capital.

And then there's the problem of the European Central Bank, which, after buying up Italian and Spanish bonds, is struggling to salvage its reputation. Germany's slow growth could make that task harder, if a German pullback from Europe's problems forces the ECB to soak up of Europe's shaky government bonds. That could also worsen strains within the union, if [Germans start rejecting the ECB](#) for doing a job they're trying to refuse. All these outcomes would bode poorly for global market confidence, which has

already nosedived because of troubles in Europe, slowing U.S. growth prospects, and a disruptive U.S. debt downgrade.

(**MORE:** [Will Italy Bring Down the Eurozone?](#))

But there's an important missing detail in all these troubles: just how much impact does German growth have on greater Europe and the global economy? According to [IMF economists Hélène Poirson and Sebastian Weber](#), not that much. Their recent research on the "spillover effects" between different economies shows the connections aren't that clear. Germany does have some influence over the growth of its biggest European trade partners, they find, but for crisis-prone countries like Greece and Italy, the "spillovers" of economic strength in Germany are pretty low.

Our main finding is that outward spillovers from Germany's growth to other countries have been low and have remained modest in recent years. In contrast, spillovers, especially from the US, followed by the UK as a distant second, have been larger and have increased over time, even after controlling for the effect of outsized spillovers during the crisis.

In fact, according to Weber and Poirson, growth in Germany is powered by the global economy, not the other way around. This has some interesting implications for Germany's role in reviving greater Europe. If Germany's and Europe's growth aren't that connected, is Germany responsible for Europe's revival? Whether the Germans like it or not, I'd venture the answer is still yes. The real risk to Europe isn't whether Germany can grow; it's whether the union can stay intact and convince the world this kind of crisis won't reoccur. To do that, Europe needs greater integration, politically and economically, which means more insurance against member countries defaulting and more central control over countries' budgets. Unfortunately, the [Franco-German proposals out today](#) lacked needed details on measures like these to soothe jittery global markets. Of course, [as TIME's Bruce Crumley notes](#), German Chancellor Angela Merkel is still hedging her bets because of [rising domestic opposition](#) to putting Germany on the hook.

So if Europe collapses on rising fears and takes the global economy with it, don't blame Germany for lackluster growth. Blame it for cowardly politics.

1 comments

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There is no way that the EU, ECB, IMF or any combination of the three, will have the ability to bail out Italy particularly with Germany's economy stalling (and most likely contracting by now).

Italy, the holder of the world's third largest debt in nominal terms, has the world's eleventh highest debt-to-GDP ratio and is unlikely to reduce its debt-to-GDP ratio to less than 115 percent even with massive cuts to its annual deficits as shown here:

<http://viableopposition.blogspot...>

Should the remainder of the Eurozone economies contract, Italy will most likely be forced to default, an action that would send...

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