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German Exports: A Booming World Will Not Replace the Eurozone

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During the eurozone crisis, Germany experienced lagging demand from the area and expanded its trade connections to emerging markets, such as China, Brazil and India. Despite the impression this creates, this is not the beginning of a deeper reorientation of German economic interests. Analysis shows that the recovering eurozone will remain the most important region for German exports. This matters for a Poland concerned not only about the destabilising effect of German disengagement from the eurozone and EU affairs but also about Warsaw's own place in the EU export chain.

In recent years, Berlin has been pressed, particularly by southern EU members, to pledge greater financial means to assistance programmes for stricken eurozone economies. Southerners have backed up their demands with the argument that the Federal Republic has been in particular a winner of the euro project, using the eurozone as a captive market for German goods, thus benefiting from southerners' indebtedness. The crisis, they say, now demands some kind of payback in the form of a "transfer union," rather like Common Agricultural Policy counterbalanced the free trade area for industrial goods under the European Communities at the end of the 1950s.

Few in Germany have been receptive to this idea. The outgoing government avoided discussion on transfers and focused instead on aid packages for individual EU members or on the Competitiveness and Convergence Instrument and saw them pushed through with little debate. One reason for Germany's reluctance was the growing eurosceptic counter-logic that if the cost of eurozone membership became too high (read transfers), Germany should consider an exit, with possible losses from the eurozone compensated for by successes in emerging economies such as China and India. Thus, even amongst mainstream parties, the monetary union is viewed sometimes less as an opportunity for German businesses as much as an ideologically-motivated sacrifice in favour of European unification.

The Eurozone's Continued Place in German Trade. Superficially at least, arguments about the viability of relying on emerging economies make sense. In 2000, more than 44% of German products were exported to other countries in the euro area. Just before the crisis in 2008, this figure had dipped slightly to 41%, although with Germany's growing export rate absolute numbers remained high. But the crisis made a significant shift in German exports: at current rates, only 35% of German products are now delivered to the eurozone. The new focus of German export policies is clear: China, Russia, Turkey, South Korea and Brazil are now in the top 20 destination countries.

This trend chimes with the numerous predictions that in a few decades the world economy would be dominated by today's emerging markets. This shift, however, should not obscure the fact that members of the eurozone still constitute the prime market for German goods. France accounts for 9.5% of all German commodity purchases abroad, the Netherlands has 6.5%, Austria has 5.3%, and Italy has 5.1%. The largest trade surpluses also are racked up with European partners. Even if there is little chance of returning to the old proportions, the relative decline of the euro area in German trade statistics will likely bottom out as the eurozone economy recovers, and especially if the emerging economies head into reverse.

The Potential Decline of Emerging Markets. Domestic demand in emerging economies is fragile, as indeed are their whole economic structures. Recent events—speculation about the end of the U.S. Fed's "quantitative-easing" programme, which destabilised the Indian rupee, and the weakness of the Brazilian real—constitute good examples of

these economies' exposure to turmoil on the currency markets. This, combined with signs of overheating, dependency on foreign capital, and rising labour costs and debt, is cause for reflection. In fact, many of these countries, notably China and Brazil, face a so called middle-income trap—too wealthy to base their competitiveness on low costs, but insufficiently innovative to challenge the developed economies. Sustainable growth will require strenuous educational reforms, the creation of new technologies, political stability, and the absence of wars or ethnic conflicts—so, enough factors to cloud even the most optimistic forecasts.

Even successful reforms might, moreover, threaten demand for German imports. In order to escape the middle-income trap, the emerging market economies must redesign their growth strategies. This means weaning themselves off imports of semi-advanced products, and shifting instead to domestic production through massive public subventions. Germany is dramatically exposed to such policies. It mainly exports industrial goods of high quality and for a high price, but they are not necessarily radical innovations. Ominously, Brazil has been focusing on cheap generic pharmaceuticals (Germany's second-largest export branch) and subsidized Chinese companies are offering stiff competition to German car producers (about 14% of German exports). A similar pattern has already led to the collapse of the German solar-panel industry.

This shows how Germany—an economic giant but a moderate player on the world stage—is already finding it hard to put international rules in place to safeguard intellectual property rights and thus export its bestsellers. The problem is being compounded by international technological breakthroughs. A combination of rising transportation costs in the global economy, combined with new production technologies, most obviously 3D-printing, would pose a serious risk to Germany's global export ambitions. Its exports, based primarily on "heavy" products of machine industry and manufacturing, can simply be replaced by computer-aided design (CAD) files sent to remote destinations in the world. Germany's small and medium-sized enterprises, which have built up their competitiveness on their ability to coordinate sophisticated industrial processes, are particularly endangered. And with them German jobs.

Recommendations. In short, the eurozone market will almost certainly remain the bedrock of German export activities. The ongoing crisis has not changed the fact that the exchange risk for German business in the eurozone is zero, costs of access are low, transport infrastructure is good, political stability is high, and demand has remained quite stable thanks to high levels of private wealth. This in turn translates into deeper economic and political cooperation, which is important if Berlin wishes to increase its global political clout. Even if there were a sustained boom overseas, Germany would not put at risk the gains of European integration, in fact, just the opposite—there are more incentives to boost help for recovering crisis-hit countries and strengthen the eurozone through financial packages and combined institutional reforms, prompting most notably a recovery in demand for German goods.

Poland would face this scenario with relief, but without joy. The crisis in the eurozone has created two extremes of risk for Warsaw. On the one side, there is the risk that the common currency may collapse into a probable chain-reaction that endangers the entirety of regional integration construction. On the other hand, there is the threat that a successful rescue of the currency transforms the eurozone into a genuine economic and political union, leaving Poland—a non-eurozone member—deeper in the periphery of the EU. An active German commitment to transfer mechanisms would offset the first but likely deepen the second. Moreover, a transfer union would not solve the underlying problems of eurozone indebtedness, trade imbalance, and lack of industrial competitiveness.

As for this last problem, Germany's efforts to build its global export portfolio may provide the answer. Berlin's support for domestic companies seeking to build their global competitiveness is worth imitation. Germany shows that a high level of productivity and innovation must be complemented by a broad network of economic associations, bodies, chambers, authorities, representations abroad, and banks, all of whom deal with the production of global exports. This is a particularly salient point for Poland, which is still short of businesses with a well-established presence on the global stage after years of focusing on the EU market. Thus, Poland' authorities and business associations may consider emulating the German system of foreign business activity planning, even if costs would be high and the effects not appear for several years.

As it stands, however, Germany's growing foreign trade, coupled with its lack of international political clout, leave it and the EU as a whole, politically exposed. A particular case of concern for Poland is Russia, which uses access to its domestic market as clout in tit-for-tat deals. In German export statistics, Russia is in 11th place, just behind Poland. However, if Russia climbs to sixth or seventh and combines that with Germany's deep dependency on energy imports, the exposure would rise and the political effects could be worrisome. The scheme could be repeated in relations with China, not only an export superpower but also a huge domestic market. China has already started a sophisticated game of putting German companies in China under pressure then offering Germany political cooperation. Poland should carefully watch such developments.