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DIW Weekly Report

36–38 2026

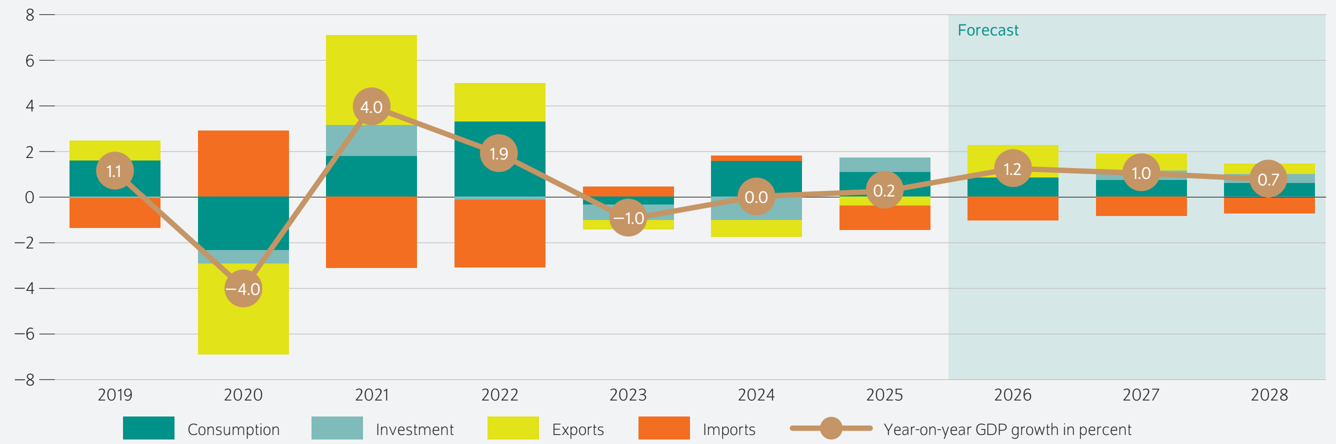
AT A GLANCE

German economy grows, but not on its own strength—global economy stays on course

By DIW Berlin's economic forecasting team

- German economy proving more resilient than expected in early summer, above all thanks to unexpectedly strong exports and expansionary fiscal policy
- DIW Berlin raises its economic forecast substantially and expects growth of 1.2 percent this year, 1.0 percent next year, and 0.7 percent in 2028
- But the recovery rests on shaky ground: high gas prices, low water levels, and structural weaknesses are slowing the economy in the second half of the year
- Setbacks also loom should the Strait of Hormuz remain closed for longer or the investment boom in artificial intelligence end abruptly
- Global economy likely to grow by 3.2 percent in both 2026 and 2027, and by 3.4 percent in 2028

German economy: Export surprise lifts growth, domestic demand yet to get going



Source: DIW Economic Forecast Autumn 2026.

FROM THE AUTHORS

"The German economy is recovering better than expected this year, but still rests on shaky ground. The rise in oil prices turned out to be surprisingly moderate despite the Iran war, while exports were supported by special factors. Neither, however, is likely to last."

—Geraldine Dany-Knedlik—

MEDIA

Audio Interview with Geraldine Dany-Knedlik (in German)
www.diw.de/mediathek

German economy grows, but not on its own strength—global economy stays on course

By Geraldine Dany-Knedlik, Nina Maria Brehl, Angelina Hackmann, Pia Hüttl, Konstantin Kholodilin, Laura Pagenhardt, Jan-Christopher Scherer, Teresa Schildmann, Hannah Magdalena Seidl, Ruben Staffa, Kristin Trautmann, and Jana Wittich

EXECUTIVE SUMMARY

The German economy has proved more resilient this year than expected in early summer. The energy price shock from the Iran war has been milder than assumed. Despite the unprecedented supply outage in the Gulf region, oil prices rose only moderately, as supply was expanded elsewhere at the same time. Natural gas is a different story: prices there are now expected to be higher than assumed in the summer, and low storage levels are likely to make themselves felt in early 2027. A vigorous recovery therefore rests on shaky ground.

Gross domestic product expanded by 0.3 percent in the second quarter, driven largely by foreign trade. Exports rose unexpectedly strongly, by 2.0 percent, above all chemical and mineral oil products—most likely a pull-forward effect prompted by the uncertainty on energy markets. Domestic demand, by contrast, stayed subdued. Private consumption rose by just 0.1 percent, investment in machinery and equipment fell by 1.4 percent, and employment continued to decline. In the third quarter, economic output is likely to be roughly flat: low water levels on important rivers are hampering transport and production in the energy-intensive sectors, and high energy prices are dampening activity further.

Thanks to expansionary fiscal policy, price-adjusted gross domestic product should grow by 1.2 percent this year, and by 1.0 and 0.7 percent in the two years after that. DIW Berlin is thus raising its expectation for the current year by more than 0.5 percentage points against the summer forecast, almost entirely on the back of those unexpectedly strong second-quarter exports. Exports are unlikely to keep up that pace, though, as structural weaknesses such as declining competitiveness in key markets like China are still there. The robust global economy should at least support demand from abroad. DIW Berlin expects global output to grow by 3.2 percent both this year and next, and by 3.4 percent in 2028. Higher energy prices are weighing on activity in many places, but the investment boom in artificial intelligence and rising military spending are propping up demand at the same time—and as a producer of intermediate goods, the German economy stands to benefit from precisely that.

All in all, the recovery now under way remains a matter for the public sector, while Germany's private sector is picking up only sluggishly. Consumer price inflation, at 2.7 percent this year and 2.6 percent next, is still well above the European Central Bank's target. The central downside risk has meanwhile shifted from the oil market to the gas market: at the end of August, German gas storage facilities were only around 52 percent full. A cold winter or a renewed geopolitical escalation would keep inflation elevated for longer and dampen private demand.

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German economy: Export surprise lifts growth, domestic demand yet to get going

The German economy has proved more resilient this year than was expected in early summer. Overall economic activity rose strongly in the first half of the year. The continuation of this vigorous recovery, however, rests on shaky ground.

The energy price shock triggered by the Iran war turned out to be considerably milder than expected in the DIW Economic Outlook Summer. Although the war in the Gulf region caused a historically unprecedented supply outage, oil prices have risen comparatively moderately. This is because global oil supply was expanded at the same time, among other things through the coordinated release of strategic reserves and through additional volumes following the easing of sanctions. Some quantities also probably left the region via alternative transport routes or on vessels outside official statistics. Price expectations for crude oil over the coming years have recently declined again. By contrast, significantly higher prices are expected for gas (Box 1). Low gas storage levels in Germany, together with the delayed pass-through of gas price increases, are therefore likely to become noticeable from the turn of the year.[1]

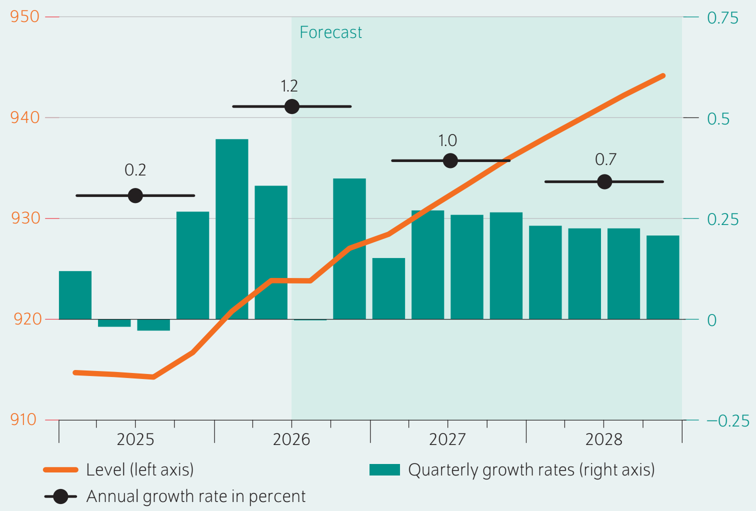
The strong economic performance in the first half of the year was driven by sharply rising exports, which are likely partly attributable to special effects. In the second quarter, foreign demand increased for crude-oil-intensive intermediate products from the chemical industry—possibly in order to hedge against further rises in energy prices. The increase is therefore likely to reflect sustainably stronger foreign demand only in part. Structural weaknesses in the German economy, such as the industrial sector's eroding competitiveness and high production costs, remain in place for now. The recovery in the second half of the year is also dampened by the low water levels over the summer on rivers that are important for the domestic economy, which have hampered the transport of goods and constrained industrial production.

The fact that the German economy is now in better shape than expected before the summer is due not least to the Federal Statistical Office revising the first-quarter figures noticeably upwards.[2] A perceptible acceleration in domestic private consumption and private investment has so far failed to materialise, however. The German economy is being carried mainly by public demand, propelled by expansionary fiscal policy (Box 2). That is likely to remain the case for the time being.

Figure 1

Growth of real GDP in Germany

In billions of euros (left axis) and quarter-on-quarter in percent (right axis)



Note: Forecast from the third quarter of 2026 onward; adjusted for price, seasonal and calendar effects.

Sources: Federal Statistical Office; DIW Berlin Economic Outlook Autumn 2026.

The German economy looks set to grow more strongly this year and next than expected back in the summer.

Second quarter: exports provide support, domestic demand subdued

After an already strong start to the year, gross domestic product (GDP) expanded again in the second quarter, by 0.3 percent (Figure 1). This increase was largely driven by foreign trade. Exports rose markedly and unexpectedly, by 2.0 percent. Exports to the rest of Europe in particular increased, including chemical products and mineral oil products, likely driven by pull-forward effects in the face of the uncertainty on energy markets caused by the Iran war. A lower dependence on intermediate products from the Gulf region compared with Asian competitors—such products having become less readily available as a result of the Iran war—probably also played a role. Data processing equipment as well as electrical and optical devices "Made in Germany" were likewise exported to the rest of Europe in greater volumes than in the previous quarter; a connection with the globally accelerating

1 The cut-off date for this forecast is August 27, 2026. Additional figures and tables can be found at www.diw.de/konjunkturzahlen. This forecast was prepared in part with the assistance of AI applications.

2 Substantial upward revisions to the official statistics also change the fundamental picture of economic developments in recent years, particularly for 2024. For that year, the Federal Statistical Office now reports stagnation instead of a decline of 0.5 percent, so that the German economy no longer contracted for two consecutive years. Growth rates for private consumption and government consumption were raised markedly; in retrospect, investment also turned out somewhat more favourably. Gross value added in manufacturing declined much less sharply than previously reported—the impression of a massive industrial weakness is thus somewhat softened and shifts towards a broader economic weakness in 2024.

Box 1

Assumptions and underlying conditions

This forecast is based on assumptions about the path of key interest rates, exchange rates, and commodity prices (Table). They are formed on the basis of developments to date, prices on futures markets, and closing levels as of the assumption cut-off date of August 13, 2026.

The Iran war has led to marked price increases on the crude oil and gas markets. Peace negotiations in the interim did cause energy prices to fall significantly for a time. After the negotiations failed, however, they rose again. On the basis of futures market prices, it is assumed that the price of Brent crude will initially remain at its elevated level in the third quarter and decline again over the forecast horizon. It will nevertheless remain above the level seen before the war began. On average, this yields a price of 85 US dollars per barrel in the current year, 77 US dollars per barrel next year, and 73 dollars per barrel in 2028. A lower crude oil price is thus assumed compared with the summer forecast: by about nine percent for the current and five percent for next year.

Table

Forecast assumptions

		2025	2026	2027	2028
ECB deposit facility[1] (year-end)	Percent	2.0	2.5	2.5	2.25
ECB key interest rate (year-end)	Percent	2.15	2.65	2.65	2.40
Money market interest rate	Three-month EURIBOR in percent	2.2	2.4	2.9	2.8
Capital market interest	Yield on euro-area government bonds with a remaining term of ten years	3.1	3.5	3.6	3.6
Capital market interest	Yield on German government bonds with a remaining term of ten years	2.7	3.1	3.1	3.1
Exchange rate	USD/EUR	1.15	1.15	1.15	1.15
Crude oil price	USD per barrel	68.0	85.0	77.1	73.5
Gas price	EUR per megawatt hour	36.3	50.4	43.5	30.4

1 The ECB is currently steering the economy via the deposit facility, not the main refinancing rate.

Note: Annual averages; year-end ECB deposit facility values.

Sources: European Central Bank; European Money Markets Institute (EMMI); Eurex Exchange; Deutsche Bundesbank; Federal Reserve; Energy Information Administration (EIA); Intercontinental Exchange (ICE); CME Group; DIW Berlin Economic Forecast Autumn 2026.

Wholesale gas prices (TTF) have also risen sharply as a result of the Iran war and at times doubled compared with the pre-war level. This forecast assumes that gas prices will continue to rise into the fourth quarter of 2026. Empty storage facilities that need to be filled for the winter are likely to favour this development. Next year, gas prices are assumed to fall gradually. As an annual average, this yields 50 euros per megawatt hour for this year, before prices fall to 43 euros in 2027 and 30 euros per megawatt hour in 2028. The gas price assumptions have thus been raised by around nine percent for the current year and 15 percent for next year compared with the summer forecast.

The higher energy prices have already fed through noticeably into consumer prices. Inflation in the euro area currently stands at 2.8 percent and is thus above the European Central Bank's (ECB) two percent target. The ECB responded to the price shock in the second quarter with an interest rate increase of 25 basis points. This forecast assumes that key interest rates will be raised by a further 25 basis points following the upcoming Governing Council meeting, so that the deposit rate is likely to reach 2.5 percent in the third quarter. By the end of 2027, the energy price shock should have largely subsided. Against this background, it is assumed that the ECB will lower the deposit rate to 2.25 percent in the first quarter of 2028. In line with key interest rates, money market rates have also risen and are likely to remain just under three percent. The interest rate increase will also become apparent in refinancing costs for households and firms. It is further assumed that capital market rates will remain largely unchanged over the forecast horizon at 3.1 percent for Germany and 3.6 percent for the euro area. The assumptions on capital market rates have thus not changed compared with the summer forecast.

The euro has recently appreciated again against the US dollar and now stands at 1.15 dollars. It is assumed that the exchange rate will remain at this value over the forecast period. This forecast is also based on assumptions regarding trade policy.[1]

1 See the section on the global economy.

expansion of data centres for artificial intelligence suggests itself here. Imports rose somewhat less strongly, by 1.5 percent, so that foreign trade contributed 0.2 percentage points to economic growth overall (Table 1).

Domestic demand, by contrast, remained subdued. Private consumption rose only marginally, by 0.1 percent, held back by a decrease in real disposable incomes compared with the previous quarter and by a persistently high propensity to save among private households (Box 3). The still weak labor market performance is also likely to have dampened consumer sentiment: while unemployment again rose only slightly, the number of people in employment fell by around 50,000 for the fourth consecutive quarter. Following a strong first quarter, public consumption likewise expanded only weakly between April and June, by 0.1 percent (Figure 2). Investment declined, as private investors in particular continued to act cautiously. Only in the area of other capital assets, which includes purchases of software, was there a noticeable increase in investment (up 0.8 percent). Investment in machinery and equipment fell by 1.4 percent, and construction investment was almost flat (up 0.1 percent). Residential and commercial construction again declined markedly, likely due not least to considerably higher construction prices. Only

Table 1

Quarterly data on the development of use and value-added components of real GDP in Germany
In percent (quarter-on-quarter, seasonally and calendar adjusted)

	2025				2026				2027				2028			
	I	II	III	IV	I	II	III	IV	I	II	III	IV	I	II	III	IV
Private consumption	0.6	−0.1	−0.1	1.0	−0.6	0.1	0.0	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Government consumption expenditure	−0.7	0.8	0.8	1.2	0.9	0.1	0.5	0.6	0.7	0.5	0.4	0.4	0.3	0.4	0.4	0.5
Gross fixed capital formation	0.3	−1.1	0.2	1.2	−1.3	−0.2	0.4	1.0	0.2	0.5	0.5	0.5	0.6	0.6	0.6	0.7
Construction	0.7	−1.2	−0.5	0.6	−1.8	0.1	0.1	0.1	0.3	0.4	0.4	0.4	0.5	0.5	0.5	0.6
Equipment	−0.2	−2.0	1.1	2.8	−1.7	−1.4	0.6	2.7	−0.5	0.5	0.6	0.6	0.6	0.6	0.7	0.7
Other fixed assets	−0.1	0.5	0.7	0.5	0.3	0.8	0.7	0.8	0.8	0.8	0.8	0.8	0.8	0.8	0.8	0.8
Inventory changes[1]	−0.1	0.8	0.0	−0.5	0.1	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Domestic demand	0.1	0.7	0.2	0.5	−0.3	0.1	0.2	0.4	0.2	0.3	0.3	0.3	0.3	0.3	0.3	0.3
Net exports	0.0	−0.7	−0.2	−0.2	0.7	0.2	−0.2	0.0	−0.1	0.0	0.0	0.0	0.0	−0.1	−0.1	−0.1
Exports	1.5	−1.2	−0.7	−0.1	2.4	2.0	−0.4	0.3	0.3	0.5	0.5	0.5	0.4	0.4	0.4	0.4
Imports	1.6	0.6	−0.2	0.5	0.5	1.5	0.1	0.4	0.5	0.5	0.5	0.5	0.6	0.6	0.6	0.6
GDP	0.1	0.0	0.0	0.3	0.4	0.3	0.0	0.3	0.2	0.3	0.3	0.3	0.2	0.2	0.2	0.2
Gross value added	0.4	−0.1	0.1	0.3	0.3	0.4	0.0	0.3	0.2	0.3	0.3	0.3	0.2	0.2	0.2	0.2
Manufacturing	0.7	−0.4	−0.7	0.1	0.5	0.9	−1.0	0.6	0.1	0.2	0.2	0.2	0.1	0.1	0.1	0.1
Construction	0.6	−1.9	−0.4	−0.5	−0.6	−0.1	0.2	0.2	0.3	0.4	0.4	0.5	0.5	0.5	0.5	0.6
Trade, hospitality, transport	0.6	−0.3	0.3	−0.2	0.5	0.3	0.1	0.1	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2
Business services	0.4	0.2	−0.2	−0.1	0.3	0.3	−0.1	0.3	0.1	0.2	0.2	0.2	0.2	0.2	0.2	0.2
Public services, education, health	0.3	0.2	0.3	0.9	0.3	0.6	0.5	0.4	0.4	0.4	0.4	0.4	0.3	0.3	0.3	0.3

1 Contribution to growth in percentage points.

Note: Forecast from the third quarter of 2026 onward.

Sources: National Statistical Offices; DIW Berlin Economic Outlook Autumn 2026.

public construction increased significantly; civil engineering in particular saw much higher investment, probably following the extensive government infrastructure measures.

Developments in consumption, investment, and foreign trade—that is, the expenditure components of GDP—are mirrored on the production side. Gross value added rose markedly again in the second quarter, by 0.4 percent. Manufacturing expanded surprisingly strongly, by 0.9 percent. This was driven by chemical production and the manufacture of electrical equipment, i.e. the same sectors that also drove the rise in exports. In line with the stagnation in construction investment, gross value added in the construction sector contracted for the fifth quarter in a row, though only marginally (by 0.1 percent). The fact that the downward momentum of recent quarters eased is likely due in large part to the government infrastructure measures. In the service sectors, economic output expanded overall. The information and communication sector posted a clear increase (up 0.6 percent), having already been expanding vigorously since the middle of last year. The intensified use of artificial intelligence is likely to be reflected here. Growth in public services was also strong again, despite weaker government consumption (up 0.6 percent). Where developments hinge on the purchasing power of private households, by contrast, momentum was weak; in the hospitality sector, value added even fell by 1.8 percent.

Third quarter: low water levels and high energy prices weigh on the economy

Business sentiment brightened at the start of the second half of the year. The ifo Business Climate index rose for the fourth consecutive month in August, and the Purchasing Managers' Index (PMI) was once again above the expansion threshold of 50 points. This improvement is driven above all by the manufacturing sector, where the PMI reached a multi-year high. For service providers the picture is mixed: while the ifo index rose here too, the PMI declined and is now below the expansion threshold. Labor market indicators have improved slightly of late but remain weak. Business confidence is thus not yet carrying over to private households. Consumer sentiment remains gloomy in view of high prices and the strained labor market situation.

Economic output is expected to be roughly flat overall in the third quarter. Developments are being impaired, on the one hand, by low water levels on important rivers, which in many places are hampering production through shortages of intermediate goods and transport constraints. This particularly affects export-bound goods from energy-intensive industries, above all chemicals and metal production. On the other hand, the high energy prices resulting from the Iran war are likely to have a dampening effect, albeit a weaker one than assumed in the summer. A decline in production in the energy-intensive sectors was already becoming apparent in June.

Box 2

Assumptions on fiscal policy measures

Fiscal policy is expansionary in the current and the coming year; in 2028, by contrast, it is likely to be almost neutral in cyclical terms (Table).

On the revenue side, adjustments to the income tax schedule continue to provide relief to private households across the entire forecast horizon. Because the relieving elements of the income tax reform expected to enter into force on January 1, 2027, will only partly take effect, whereas the burdensome counter-financing measures take hold more quickly, the reform generates a stronger expansionary impulse in 2028 than in 2027. Businesses benefit throughout the forecast period from the tax relief provided by the immediate investment programme, which from 2028 onwards includes not only direct investment incentives through more generous declining-balance depreciation, but also a step-by-step reduction in corporate income tax. The hospitality sector continues to be relieved by the permanent reduction of value-added tax to seven percent, albeit with diminishing effect, and agricultural businesses benefit from the rebate on agricultural diesel expenses in 2026. The temporary reduction in the energy tax on fuels in May and June of this year on account of the Iran war has a mechanically restrictive effect next year.

The step-by-step increase in tobacco tax generates a moderate restrictive impulse in all years of the forecast horizon. Revenues from fuel emissions trading (BEHG) rise noticeably this year, as the price per tonne of CO2 increased by ten euros at the turn of the year to the upper limit of 65 euros of the defined national corridor. By assumption, it remains there in 2027 and 2028.[1] The global minimum tax (Pillar 2) also contributes to additional revenue in 2026, and from 2027 onwards it is assumed that the EU plastics levy, hitherto borne by the state, will be passed on to businesses and consumers. Also newly added from 2027 is a tax on sugary drinks. Despite these measures, the relief for businesses and households predominates overall, such that fiscal policy on the revenue side of central, state, and local government is moderately expansionary in all years of the forecast horizon.

On the social insurance side, the further rising average supplementary contribution to statutory health insurance has a strongly restrictive effect in the current year and again in 2028, while the contribution rate in 2027 can, by assumption, be kept constant thanks to the statutory health insurance contribution rate stabilisation act passed in the summer of 2026. In addition, further increases in the contribution rate to statutory long-term care insurance are assumed for 2027 and 2028. For 2028, a significant increase in the contribution rate to the statutory pension insurance is also emerging. Overall, the fiscal stance on the revenue side of the social insurance funds becomes increasingly restrictive over the forecast period and fully offsets the tax relief in 2028.

The design of fiscal policy on the expenditure side of government initially retains a clearly expansionary character over the forecast horizon, even though individual consolidation measures generate restrictive impulses. Cuts to housing benefit and parental allowance dampen expenditure. Set against this, additional expenditure arises from the increase in child benefit—as part of the 2026 income tax reform—as well as from the Start Opportunities programme for schools. From 2027 onwards, the BAföG reform adopted by the cabinet is added. The largest expansionary impulses continue to come from the expanded borrowing scope for infrastructure and defence. Rising funds continue to be disbursed from the special fund for infrastructure and climate neutrality (SVIK) in all years of the forecast horizon, albeit at a decreasing pace. Equipment ordered under the Bundeswehr special fund is increasingly being delivered and the sectoral exemption for defence is being drawn on with further momentum, such that defence spending rises noticeably in all years. The additional financial support for Ukraine still has an expansionary effect in the current and the coming year, but will be scaled back in 2028 and will then generate a restrictive impulse. The Climate and Transformation Fund (KTF) finances the subsidisation of grid fees from the current year onwards, as well as, from 2027, the industrial electricity price intended to dampen electricity prices for energy-intensive companies. The impulses from the remaining KTF programme expenditure vary over the forecast horizon (expansionary in 2027 and restrictive in 2026 and 2028).

On the expenditure side of the social insurance funds, expansionary impulses in the current year come from the removal of budget caps in primary care, the act on support and relief in long-term care, and the hospital reform; the latter is assumed to produce initial savings effects only in 2028 and then has a restrictive effect. The extended duration of short-time work benefits expires at the turn of the year 2027. However, since short-time work is currently little used as an instrument, the resulting restrictive impulse is small. Of considerable weight will be the adopted, and partly retroactive, expansion of the mothers' pension, which leads to addition-

1 This is a conservative assumption, based on the fact that the CO2 price in this area is subject to high uncertainty in 2028. In 2028, the BEHG will be transferred into the European emissions trading system ETS2. The certificate price will then in principle be determined by the market, without a corridor. A reserve is intended to have a price-stabilising effect through the issuance of additional certificates if the certificate price exceeds €45, but it is unclear whether the price can be fully pinned at that level.

Weak production is likely to result in a renewed decline in already lacklustre private investment activity in the third quarter. Exports, too, are projected to fall again in the absence of the second quarter's pull-forward effects and with the transport constraints caused by low water levels. Private consumption is likely to stagnate given persistently high inflation and weaker income growth. In residential construction as well, real gains are unlikely to materialise because of the intensified price pressure. Public spending alone is likely to continue supporting activity (Table 2).

Table

Fiscal policy measures: burdens (−) and relief (+) by the general government budget
In billion euros (compared to the previous year)

	2026	2027	2028
Revenues of central, state, and local government			
Annual Tax Act 2022	−0.2	−0.2	−0.2
Inflation Compensation Act (adjustment of income tax rates)	−0.6	−0.5	−0.6
Income Tax Reform 2026	0.0	−2.9	−4.1
Tax Amendment Act 2025 (excluding value-added tax)	0.0	−1.1	−0.9
Tax Law Development Act	−5.5	−0.9	−0.4
Annual Tax Act 2024	0.3	−0.1	0.7
Active pension (pension package)	−0.8	−0.1	0.0
Second Occupational Pension Strengthening Act (pension package)	0.0	−0.1	0.0
Declining-balance depreciation (Second and Fourth Corona Tax Assistance Acts)	3.8	1.5	0.7
Immediate investment programme	−3.4	−4.8	−6.7
Growth Opportunities Act	−0.3	−0.6	−0.6
Financing for the Future Act	−0.1	0.0	0.0
Changes to the agricultural diesel rebate	−0.4	0.0	0.0
Permanent reduction of value-added tax in the hospitality sector	−3.1	−0.6	−0.1
Temporary reduction of the energy tax on fuels	−1.4	1.4	0.0
Increase in truck tolls	0.2	0.0	0.0
Increase in tobacco tax	0.8	0.8	0.8
Air traffic tax	−0.2	−0.2	0.0
Revenues from fuel emissions trading (BEHG)	3.0	0.0	0.0
Global minimum taxation (Pillar 2)	0.5	−0.1	−0.1
Plastic tax	0.0	1.4	0.0
Sugar tax	0.0	0.5	0.0
Other tax measures	−2.5	−2.7	−2.2
Social security revenues			
Increase in average additional contribution to statutory health insurance	5.9	0.0	1.6
Statutory Health Insurance Contribution Rate Stabilisation Act	0.0	4.3	1.6
Increase in the contribution rate to the statutory pension insurance	0.0	0.0	12.6
Increase in the contribution rate to the statutory long-term care insurance	0.0	3.3	1.8
Expenditure of central, state, and local government			
Cuts to housing benefit	0.4	1.2	0.3
Cuts to parental allowance	0.1	0.4	0.0
BAföG reform	0.0	−0.2	−0.1
Increase in child benefit	−0.8	−1.8	−0.9
Start Opportunities (Startchancen) programme for schools	−0.5	−0.3	−0.3
Early-start pension (Frühstartrente)	0.0	−0.2	0.0
Subsidisation of grid fees	−6.5	1.0	0.0
Industrial electricity price	0.0	−2.4	1.2
Abolition of the gas storage levy	2.5	0.6	0.0
KTF special fund (excluding grid fees/industrial electricity price/gas storage levy)	3.8	−3.6	2.5
Additional expenditure from the special fund for infrastructure and climate neutrality (SVIK)	−12.0	−10.0	−3.0
Additional expenditure on defence (including the Bundeswehr special fund)	−14.5	−17.0	−8.0
Additional support for Ukraine	−2.8	−0.1	3.1
Social security expenditure			
Hospital reform	−0.2	−0.2	2.2
Removal of budget caps in primary care	−0.4	0.0	0.0
Act on support and relief in long-term care	−0.2	−0.3	−0.2
Extension of the duration of short-time work benefits	0.0	0.3	0.0
Mothers' pension	0.0	0.0	−10.0
Health insurance savings package 2026	2.0	−2.0	0.0
Statutory Health Insurance Contribution Rate Stabilisation Act	0.0	13.7	5.1
Total	**−33.0**	**−22.6**	**−4.2**
As a percentage of GDP	**−0.7**	**−0.5**	**−0.1**

Note: Without macroeconomic repercussions. Other tax measures: Annual Tax Act 2020, Act on the Modernisation of Corporation Tax Law, Disabled Persons Lump Sum Act, Fourth Bureaucracy Relief Act, Credit Market Promotion Act.

Sources: Federal Government (budget, draft legislation, monthly reports of the Federal Ministry of Finance, tax policy data collection); DIW Berlin Economic Outlook Autumn 2026.

al expenditure in the double-digit billions in 2028. Working in the opposite direction is the contribution rate stabilisation act for statutory health insurance (GKV) passed in the summer of 2026, which entails substantial cross-sectoral savings in the health system from 2027 onwards and thus continues and considerably reinforces the consolidation efforts operating under the name of the GKV savings package this year. Overall, fiscal policy measures on the expenditure side of the social insurance funds are neutral in 2026, restrictive in 2027, and again almost neutral in 2028.

All in all, the budgetary impact of the fiscal policy measures amounts to −33.0 billion euros in the current year (−0.7 percent in relation to nominal GDP), −22.6 billion euros in 2027 (−0.5 percent), and −4.2 billion euros in 2028 (−0.1 percent).

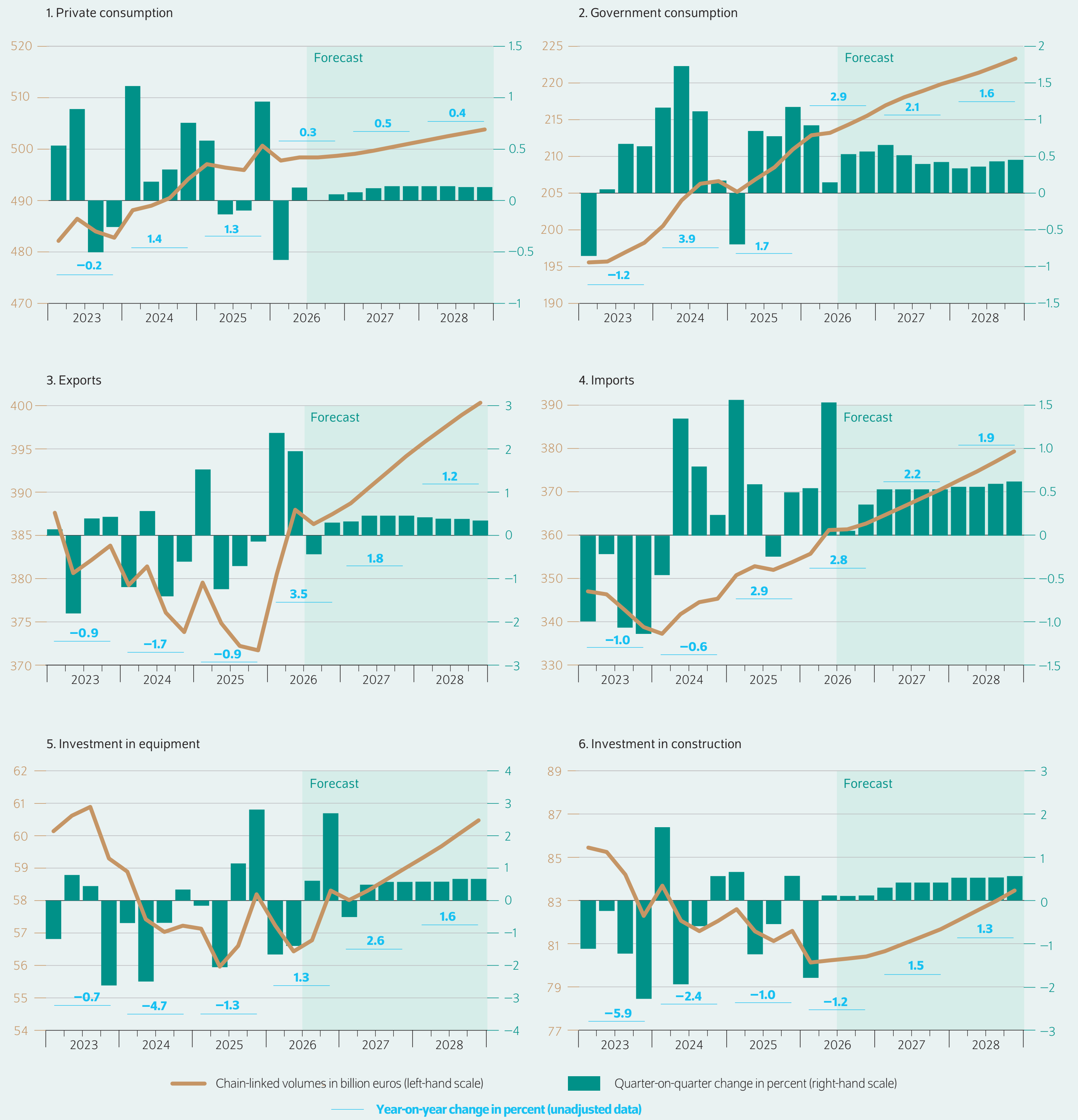
Further outlook: fiscal policy carries growth, private-sector recovery delayed

Economic policy conditions remain favourable overall over the forecast period. The European Central Bank (ECB), following a further upward step this quarter, will likely keep interest rates constant through 2027 and lower them again at the beginning of 2028. Fiscal policy will initially remain clearly expansionary. Fiscal impulses amount to around 33 billion euros this year and 23 billion euros next

Figure 2

Components of GDP

Seasonally, calendar, and price-adjusted development



Note: Forecast from the third quarter of 2026 onward; adjusted for price, seasonal, and calendar effects.

Sources: Federal Statistical Office; DIW Berlin Economic Outlook Autumn 2026.

year (Table 3). In 2028, this momentum is likely to come to a halt. The structural primary balance widens to 3.0 percent in relation to potential output by 2027 and then remains at that level (Figure 3). Net primary expenditure, which is relevant for fiscal surveillance in the euro area, rises considerably more strongly in every year of the forecast horizon than agreed in the medium-term fiscal-structural plan between the federal government and the European Commission. Even after taking the defence flexibility[3] into account, the control variable for the deviations exceeds 0.3 percent in 2027 and 2028, and, on a cumulative basis in 2028, exceeds 0.6 percent in relation to GDP (Table 4). This brings an excessive deficit procedure by the Commission against Germany into the realm of possibility.

Although the expansionary course of government is losing steam, government consumption is likely to be expanded significantly over the forecast period and to provide substantial support to GDP. The fact that the fiscal impulses are diminishing does not imply that government spending is falling. It merely means that spending is being expanded by smaller additional amounts from one year to the next, while its level continues to rise. Purchases of intermediate goods and services will likely continue to increase strongly through disbursements from the special funds and the sectoral exemption for defence. Social benefits are also rising noticeably for demographic reasons; by assumption, savings efforts are reflected only in the area of health insurance. Public investment activity, too, is expected to continue expanding strongly. Orders placed under the Bundeswehr special fund are increasingly being delivered and recorded. In civil engineering, which receives a large share of the public infrastructure funds, incoming orders and construction output have been rising markedly for years. Significant increases in public investment in machinery and equipment and in construction are therefore also expected going forward.

Meanwhile, private domestic demand is likely to continue picking up moderately. Domestic orders have stabilised recently, although they have been shaped largely by major orders, presumably mainly driven by military procurement. This benefits not only defence companies in the narrower sense, but also manufacturers in the so-called dual-use segment, whose products—such as electronics, optics, or vehicle technology—are used both for civilian and for military purposes. The increased demand for industrial goods thus permits cautious confidence. Nevertheless, Germany as a production location continues to be marked by structural obstacles, above all high energy costs, and the willingness to invest remains low, so that business investment is projected to only slowly gain momentum.

Accordingly, only a gradual recovery is to be expected on the labor market (Table 5). Rising demand should, however, increasingly utilise existing capacity and lead to employment picking up somewhat again from 2027, following the recent phase of job cuts. Real incomes are likely to continue to rise, but only moderately. Together with the persistently high propensity to save, this is reflected in subdued overall projected growth in private consumption.

3 Under the national escape clause, an additional cumulative increase in defence spending of 1.5 percent of GDP compared with 2021 is exempted.

Table 2

Contributions to GDP growth in Germany
In percentage points (price-adjusted)

	Contributions to growth[1]			
	2025	2026	2027	2028
Consumption expenditures	1.1	0.8	0.7	0.6
Private households	0.7	0.2	0.3	0.2
Government	0.4	0.7	0.5	0.4
Gross fixed capital formation	−0.1	0.1	0.4	0.4
Construction	−0.1	−0.1	0.2	0.1
Equipment	−0.1	0.1	0.2	0.1
Other fixed assets	0.1	0.1	0.1	0.1
Inventory changes	0.7	0.0	0.0	0.0
Domestic demand	1.7	0.8	1.1	1.0
Net exports	−1.5	0.4	−0.1	−0.2
Exports	−0.4	1.4	0.7	0.5
Imports	−1.1	−1.0	−0.9	−0.7
Gross domestic product[2]	0.2	1.2	1.0	0.7

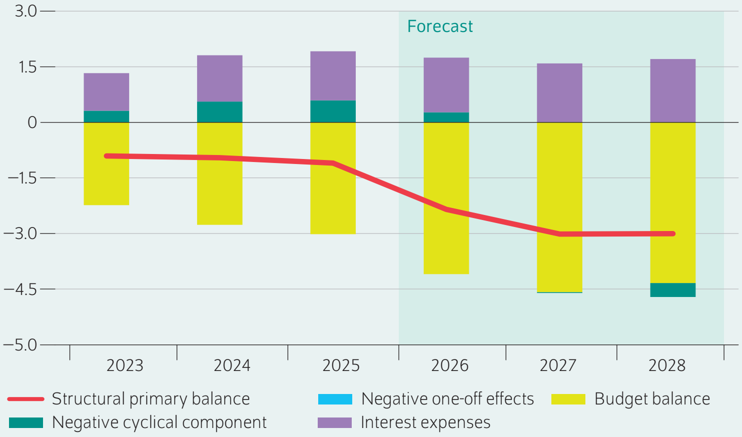
1 Year-on-year change in percent; any deviation in the totals is due to the rounding of the figures.
2 Change from the previous year in percent; differences in totals due to rounding of figures.

Note: Forecast from 2026 onward.

Sources: Federal Statistical Office; DIW Berlin Economic Outlook Autumn 2026.

Figure 3

Structural primary balance
In percent (relative to nominal potential output)



Note: The structural primary balance is the sum of the columns. Forecast from 2026 onward.

Sources: Federal Statistical Office; DIW Berlin Economic Forecast Autumn 2026.

The structural primary deficit will widen over the forecast period.

Table 3

Selected fiscal policy indicators[1]

In percent (in relation to nominal gross domestic product)

	Government revenue			Government expenditure			Budget balance	Interest-to-tax ratio[2]	Government debt ratio (Maastricht definition)
	Total	of which: Taxes	of which: Social contributions	Total	of which: Interest expenditure	of which: Gross investment			
2017	45.7	23.7	16.4	44.4	1.0	2.4	1.3	4.3	64.0
2018	46.3	23.9	16.6	44.4	0.9	2.6	1.9	3.8	60.8
2019	46.6	24.0	16.8	45.3	0.8	2.7	1.3	3.3	58.7
2020	46.4	23.0	17.5	50.7	0.6	3.0	−4.3	2.8	68.0
2021	47.1	24.2	17.0	50.3	0.6	2.8	−3.2	2.4	68.1
2022	46.5	24.0	16.6	48.4	0.7	2.9	−1.9	2.9	65.0
2023	45.5	22.6	16.7	47.7	0.9	2.9	−2.2	3.9	62.9
2024	46.2	22.7	17.3	49.0	1.0	3.2	−2.8	4.6	63.8
2025	47.2	22.8	18.2	50.2	1.1	3.4	−3.0	4.8	64.8
2026	46.8	22.4	18.2	50.8	1.2	3.4	−4.1	5.2	66.3
2027	46.6	22.3	18.3	51.2	1.2	3.6	−4.6	5.4	68.3
2028	47.2	22.4	18.8	51.6	1.3	3.7	−4.3	5.6	70.6
2028/2025	47.0	22.5	18.4	51.0	1.2	3.5	−4.0	5.2	67.5

1 As defined in the national accounts (Volkswirtschaftliche Gesamtrechnungen).
2 Government interest expenditure in relation to tax revenue

Note: Forecast from 2026 onward.

Sources: Federal Statistical Office; DIW Berlin Economic Outlook Autumn 2026.

Table 4

Net primary expenditure

In billions of euros and in percent

			2024	2025	2026	2027	2028
(1)	Government expenditure	EUR bn	2,149.4	2,274.4	2,399.4	2,514.5	2,608.3
(2)	− Interest expenditure	EUR bn	45.9	49.0	54.8	59.2	63.7
(3)	− Cyclical component of labor market expenditure (COFOG)[1]	EUR bn	0.4	7.8	9.7	8.0	5.1
(4)	− Expenditure on EU programmes[2]	EUR bn	8.5	7.8	11.9	9.0	9.0
(5)	− National expenditure on the co-financing of EU programmes[2]	EUR bn	1.7	1.6	2.0	2.7	2.5
(6)	+ One-off effects on the expenditure side[2]	EUR bn	0.0	0.0	−0.1	0.0	0.0
(7)	Net primary expenditure (NPE; before discretionary measures)	EUR bn	2,092.9	2,208.3	2,321.0	2,435.6	2,527.9
(8)	Absolute change in NPE	EUR bn		115.4	112.8	114.6	92.3
(9)	Discretionary revenue-side measures[3]	EUR bn	17.2	29.2	0.6	2.8	8.4
(10)	Adjusted absolute difference in NPE: (8)−(9)	EUR bn		86.1	112.2	111.8	83.9
(11)	**Growth rate of NPE: (10) relative to (7) of the respective previous year**	**percent**		**4.1**	5.1	4.8	3.4
(12)	**Envisaged NPE path with activation of the national escape clause as set out in the MTP**	**percent**		**4.4**	4.5	2.3	1.7
(13)	Difference between DIW and MTP: (11)−(12)	percentage points		−0.3	0.6	2.5	1.7
(14)	Absolute difference	EUR bn		−6.0	12.8	58.4	42.5
(15)	Difference relative to gross domestic product (GDP)	percent		−0.1	0.3	1.2	0.8
(16)	Cumulative absolute difference	EUR bn		−6.0	6.8	65.2	107.7
(17)	Cumulative relative to GDP	percent		−0.1	0.1	1.3	2.1
(18)	Defence flexibility relative to GDP[4]	percent		0.4	0.8	1.1	1.5
(19)	**Control variable after flexibility relative to GDP: (15)− Δ(18)**	**percent**		**−0.5**	−0.1	0.9	0.4
(20)	**Cumulative control variable relative to GDP**	**percent**		**−0.5**	−0.6	0.3	0.7

1 From 2026 onwards, DIW Berlin forecast, adjusted using the NAWRU.
2 Up to 2027, figures from the EU Commission; thereafter, DIW Berlin assumption.
3 From 2026 onwards, DIW Berlin forecast.
4 Up to 2027, figures from the EU Commission; for 2028, set at the maximum (1.5 percent).

Sources: DIW Berlin Economic Outlook Autumn 2026.

Box 3

Nowcast of labor income inequality

DIW Berlin has developed a model that can forecast labor income inequality up to the present time (so-called nowcast). The model combines annually available microeconomic data from the Socio-Economic Panel (SOEP) with a large number of higher-frequency macroeconomic and labor market indicators, as well as the current results of the DIW Economic Outlook, within a macro-econometric framework. This makes it possible to project the average labor incomes of different income groups. Based on the model results, and under certain distributional assumptions, a labor income distribution for the total population can then be constructed.

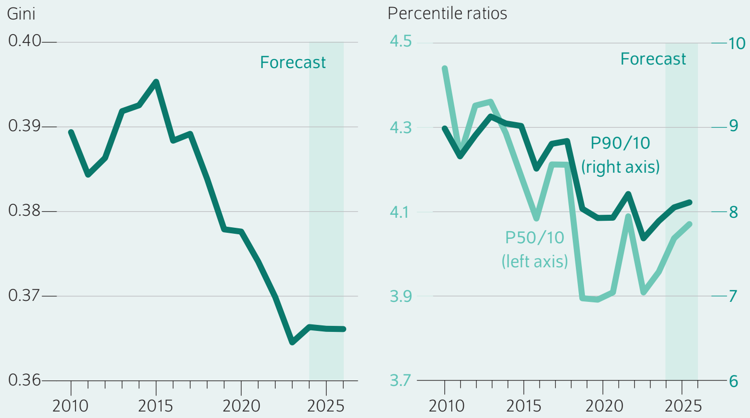
SOEP data are currently available up to 2024 (wave v41). The model is therefore used to estimate the development of inequality for 2025 and 2026. The estimate for 2025 is based exclusively on macroeconomic data from official statistics, while the nowcast for the current year also incorporates DIW Berlin's current economic forecast.

The model results show that labor income inequality has increased again since 2023, after having fallen markedly in the preceding crisis years (Figure). The Gini coefficient rises from 0.365 in 2023 to 0.366 in 2024 and has remained at that level since. The fact that inequality increased above all in 2024 is likely to be due primarily to middle- and top-earning households having benefited from wage negotiations and correspondingly strong real wage gains following the period of high inflation in 2022/23, while the increases at the lower end were likely smaller. This suggests that the fiscal stance in Germany was at least unable to prevent a slight rise in labor income inequality. This can also be seen in the fact that the income ratios between top and low earners (P90/10) as well as between the middle and the lower end of the distribution (P50/10) have likewise been rising since 2023.

Figure

Nowcast of labor income inequality: Gini index and selected percentile ratios

Index points (left side), percentile ratios (right side)



Sources: Socio-Economic Panel (SOEP); Federal Statistical Office; DIW Berlin Economic Outlook Autumn 2026.

Labor income inequality increases slightly.

Foreign trade is also expected to provide only limited impetus in the coming years. After exports rise strongly again this year, supported in part by the special effects mentioned above, their momentum is likely to weaken noticeably in subsequent years. Reduced price competitiveness, high energy costs, and dwindling demand from China are slowing German exports. At the same time, imports continue to pick up along with gradually increasing domestic demand and strong public spending.

Export surprise lifts DIW economic forecast substantially

All in all, price-adjusted GDP in Germany is projected to increase by 1.2 percent this year. Over the next two years, economic output is expected to rise by 1.0 and 0.7 percent respectively. In the current and coming year, the higher number of working days contributes 0.3 and 0.1 percentage points respectively to economic growth, while this so-called calendar effect will be negative in 2028 (−0.2 percentage points). DIW Berlin is thus raising its growth expectation for the current year considerably compared with the summer forecast, by more than half a percentage point. This upward revision is almost entirely attributable to a forecast error in the first half of the year—and that in turn largely to the unexpectedly strong exports in the second quarter. The statistical data revisions, by contrast, contribute little to the growth revision, since although they raise the level of economic output, they barely affect the rates of change. For the coming year, too, economic growth is 0.2 percentage points more positive than in the summer forecast—this is mainly due to a higher statistical carryover resulting from the stronger performance in the current year.

Growth in potential output averages around 0.3 percent in the medium term according to Modem (Modified EU Method), and is thus somewhat higher than in the DIW Berlin Economic Outlook Summer. The reasons for the upward revision are a slightly higher assumed growth in aggregate production as well as a milder decline in the volume of labor,

Box 4

Potential output

Table 1

Medium term: persons in employment, employees, and working time

In thousands of people (unless stated otherwise)

	Persons in employment (domestic)	Employees (domestic)	Working time per person in employment	Gross domestic product				
				Price adjusted, chain-linked volumes			At current prices	Deflator
				Total	Per person in employment	Per hour worked		
	in thousands	in thousands	in hours	in billions of euros	in euros	in euros	in billions of euros	2020=100
2019	45,291	41,145	1,372	3,624	80,010	58	3,558	98
2025	45,878	42,214	1,336	3,654	79,645	60	4,530	124
2031	45,410	41,854	1,334	3,816	84,043	63	5,476	143
Average annual change in percent								
2025/2019	0.2	0.4	−0.4	0.1	−0.1	0.4	4.1	4.0
2031/2025	−0.2	−0.1	0.0	0.7	0.9	0.9	3.2	2.5

Source: Federal Statistical Office, DIW Economic Outlook Autumn 2026.

The calculation of potential output is based on the procedure prescribed by the European Commission.[1] It rests on a Cobb-Douglas production function with the input factors volume of work, capital stock, and total factor productivity (TFP). Foreseeable demographic structural effects are taken into account by extrapolating and smoothing the development of the components of the volume of work for different age cohorts and subsequently aggregating them, using age shares, into an economy-wide component.[2]

For population developments, DIW Berlin draws on variant G2-L2-W1 of the 16th coordinated population projection published by the Federal Statistical Office in December 2025, which assumes moderate developments in the birth rate and life expectancy and a low net migration balance. Net immigration is likely to decline to around 100,000 people in the current year. Assuming that the migration balance corresponds to the level of variant W1 from 2027 onwards, net immigration is set at 150,000 people thereafter. The total working-age population in Germany already began to decline in 2025 in the course of demographic ageing (Table 1). Since the increased immigration of refugees in 2015, participation rates have been considered separately for refugees and for the rest of the working-age population. For 2026, a participation rate of around 70 percent is projected for all refugees. The participation rate of the rest of the working-age population is extrapolated over the medium term using an age cohort model, in order to take account of the fact that the weight of age cohorts with high labor force participation is declining for demographic reasons while that of cohorts with considerably lower participation is increasing. The economy-wide participation rate is obtained as a weighted average of the refugee participation rate, interpreted as structural, and the trend in labor force participation of the rest of the population.

Table 2

Growth of real potential output

Annual average change in percent

		Modem	EU method
	2020–2025	2025–2031	2025–2030
Potential output	0.7	0.3	0.5
Contributions to growth			
Capital input	0.3	0.2	0.3
Total factor productivity	0.3	0.3	0.4
Labor input	0.1	−0.3	−0.2
Working-age population	0.2	−0.2	−0.2
Participation rate	0.1	0.0	0.1
Unemployment rate	0.0	0.0	0.0
Average working time	−0.2	−0.1	0.0

Sources: Federal Statistical Office; European Commission; DIW Berlin Economic Outlook Autumn 2026.

1 For a detailed description of this method, see Karel Havik et al. (2010): The Production Function Methodology for Calculating Potential Growth Rates and Output Gaps. European Commission, European Economy—Economic Papers series, No. 420.

2 See Fichtner et al. (2017), Deutsche Wirtschaft bleibt gut ausgelastet: Grundlinien der Wirtschaftsentwicklung im Herbst 2017, DIW Wochenbericht No. 36, pp. 715–736.

According to this approach, it reaches its peak in 2027 and will decline thereafter. The estimation of the structural unemployment rate takes into account the particular labor market situation of refugees, but is essentially derived from the structural unemployment rate of the remaining labor force, which is determined using a Hodrick-Prescott filter. The economy-wide structural unemployment rate is accordingly likely to stand at about 3.4 percent in 2026. By 2031 it falls to 3.3 percent as a result of a declining unemployment rate among refugees.

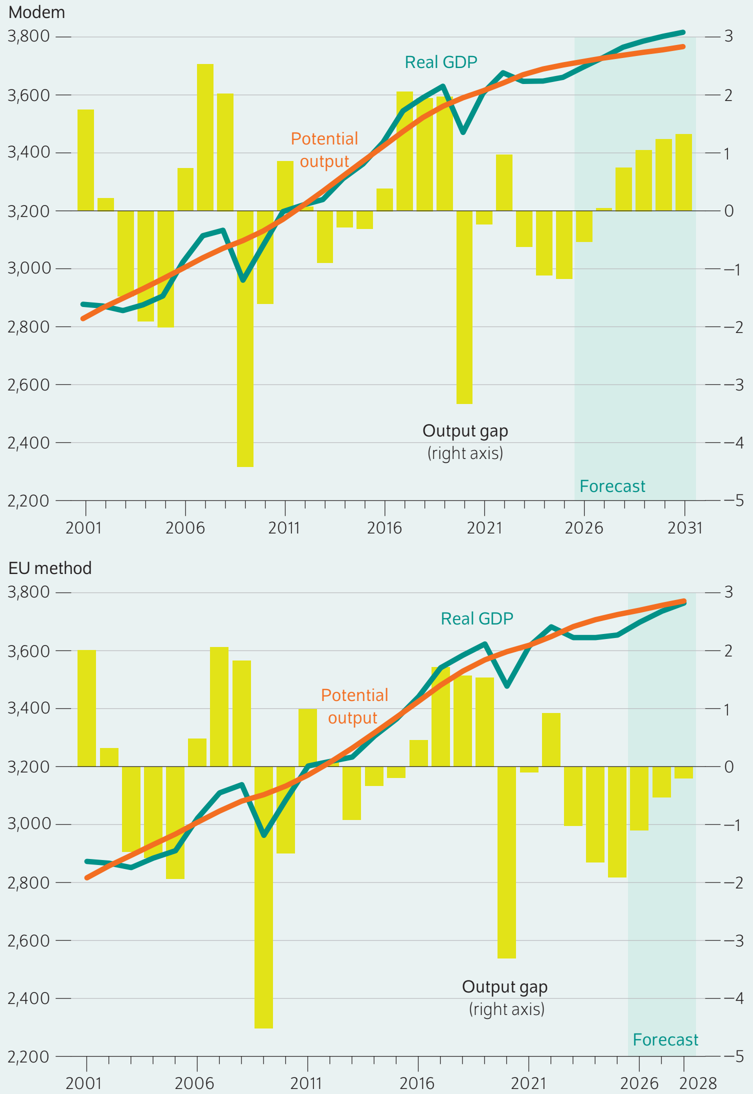
The capital stock is extrapolated over the entire projection period on the basis of increases in net investment. Accordingly, gross fixed capital formation less depreciation is added to the previous year's capital stock. The observed depreciation rate is used up to 2025 and subsequently held constant at the value of the last observation point. The capital stock is not smoothed.

According to the modified EU method (Modem), potential output will grow by an average of around 0.3 percent in the medium term, and thus somewhat more strongly than in the summer. The reasons for the upward revision are somewhat stronger assumed growth in aggregate production as well as a milder decline in the volume of work, resulting from a higher number of hours worked. According to the EU method, potential growth in the medium term is forecast at around 0.5 percent (Table 2). The output gap, which measures the degree of utilisation of aggregate capacity, is likely to stand at −0.5 percent of potential output this year according to Modem, thus indicating underutilisation. At −1.1 percent, the EU method shows considerably greater underutilisation (Figure). As the recovery continues, the gap closes over the forecast period according to Modem and is likely to turn into overutilisation towards the end of 2027. This development is likely driven above all by persistently strong public demand. According to the EU method, by contrast, the gap is expected to remain negative through to the end of the short term.

Figure

GDP, potential output and output gap

In billions of euros (left axis) and percent of potential output (right axis)



Note: Forecast from 2026 onwards.

Source: DIW Economic Outlook Autumn 2026.

The EU method shows considerably greater underutilisation for this year.

Table 5

Key economic indicators for the German economy

	2025	2026	2027	2028
GDP[1]	0.2	1.2	1.0	0.7
Employment[2] (1,000 persons)	45,878	45,684	45,687	45,821
Unemployed (1,000 persons)	2,948	2,992	2,928	2,720
Unemployment rate[3] (BA concept, in percent)	6.3	6.4	6.2	5.8
Consumer prices[4]	2.2	2.7	2.6	2.0
Unit labor costs[4,5]	4.3	2.1	2.2	2.9
Government budget balance[6]				
in billions of euros	−136.5	−192.5	−224.6	−219.0
in percent of nominal GDP	−3.0	−4.1	−4.6	−4.3
Current account balance				
in billions of euros	202.1	221.3	238.6	234.8
in percent of nominal GDP	4.5	4.7	4.9	4.6

1 Price adjusted. Year-on-year change in percent.
2 Domestic concept.
3 Unemployed as a percentage of the civilian labor force (definition according to the Federal Employment Agency).
4 Year-on-year change.
5 Compensation of employees per hour worked in Germany as a percentage of real GDP per hour worked.
6 As defined in the national accounts (*Volkswirtschaftliche Gesamtrechnungen*).

Note: Forecast from 2026 onward.

Sources: Federal Statistical Office; DIW Berlin Economic Outlook Autumn 2026.

resulting from a higher number of hours worked. The output gap, which measures the degree of utilisation of aggregate capacity, is likely to stand at –0.5 percent of potential output this year, indicating underutilisation. As the recovery continues, the gap closes over the forecast period and is likely to turn into overutilisation towards the end of 2027 (Box 4).[4] This development is likely driven above all by persistently strong public demand.

Consumer price inflation, expected at 2.7 percent this year and 2.6 percent next year, will be well above the ECB's stability target of around two percent. The milder-than-expected rise in oil prices dampens headline inflation by 0.2 and 0.4 percentage points respectively compared with the summer forecast. DIW Berlin bases its energy price assumptions on the futures markets and has lowered its oil price assumption accordingly, while the gas price assumption has been raised, as gas prices have developed less favourably of late (Box 1). Special effects such as the increase in the pharmacy fixed fee in July of this year, as well as higher co-payments in the health sector and the tobacco tax increase from 2027, additionally push prices up. However, these are temporary and do not constitute broad-based inflation. The pass-through of higher energy and agricultural production costs is also likely to be moderate. Price increases will probably peak in early 2027 and then gradually recede. In 2028, the inflation rate is then likely to be back at 2.0 percent. Core inflation is expected to remain elevated for longer owing to the persistent after-effects of the energy price shock, and to decline only gradually from mid-2027.

The risks to this forecast are considerable. The central downside risk has shifted over the course of the year from the oil market to the gas market. At the end of August, gas storage levels in Germany stood at around 52 percent, an unusually low level for this time of year. The gas price at that point was around 66 euros per megawatt hour, well above the previous-year level. A cold winter, persistently high demand from Asia, or a renewed geopolitical escalation could push gas prices even higher, keep inflation elevated for longer, and additionally dampen private demand. Furthermore, some of the burdens of the energy price shock will take effect only with a delay and could feed through more strongly in the third quarter than assumed. Beyond energy prices, a prolonged closure of the Strait of Hormuz could lead to supply chain problems and production disruptions, and a spread of the conflict to further countries or to financial markets would amplify the effects on the real economy. A key domestic risk remains the uncertainty about structural change in manufacturing. It is an open question which part of the industrial weakness is cyclical and which is structural in nature. Should the assumed revival of industry fail because of reduced competitiveness, the recovery would turn out weaker than expected.

4 For the result according to the EU-method, see also Box 4.

Global Economy Stays on Course Despite the Iran War

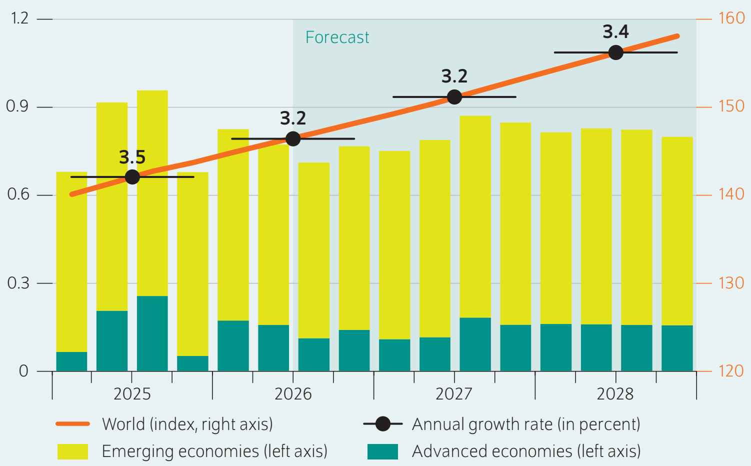
The global economy proved remarkably robust in the first half of 2026. Following growth in global gross domestic product (GDP) of 0.8 percent in the first quarter, it expanded at the same pace in the second quarter—despite severely restricted traffic through the Strait of Hormuz since the spring (Figure 4). Opposing forces lie behind this stability. The higher energy prices caused by the Iran war are dampening private consumption and energy-intensive production, while the investment boom in artificial intelligence (AI) and rising military spending in many countries are supporting demand.

Growth in the second quarter was once again driven by the emerging economies. Their pace of expansion remained almost unchanged at 1.1 percent. In China, domestic economic activity was weak: fixed investment was well below its year-earlier level, primarily because of a slump in real estate investment. Exports, by contrast, continued to support growth. Overall, China's GDP rose by 0.9 percent. India is likely to remain on an expansionary path at 1.5 percent, supported in part by strong investment in AI infrastructure. In the EU member states of Central and Southeastern Europe, growth accelerated to 0.8 percent from 0.4 percent in the first quarter, which is likely also attributable to markedly higher defense spending. Following a decline of 0.8 percent in the first quarter, Mexico grew strongly in the second quarter, by 1.5 percent. The main drivers were agriculture, services, and spending in the run-up to the FIFA World Cup. Momentum also remained stable in the advanced economies. In the euro area, growth accelerated to 0.4 percent in the second quarter after stagnating in the first. Around one quarter of the increase was attributable to Ireland, however, while Italy grew by 0.2 percent and France stagnated. Spain again grew strongly, by 0.7 percent on the quarter, driven—as in previous quarters—by private consumption and investment, particularly in the construction and intellectual property components. In South Korea and Japan, high exports of technology-intensive goods continued to support economic activity. South Korea's GDP rose by 0.6 percent in the second quarter, following an exceptionally strong increase of 1.8 percent in the first quarter. In the United Kingdom, the recovery continued: after 0.6 percent in the first quarter, the economy grew by 0.4 percent in the second, supported by corporate investment in AI and government defense investment.

Figure 4

Real GDP growth

Quarter-on-quarter percentage growth (left axis); index 2015 Q1 = 100 (right axis)



Sources: National statistical offices; DIW Berlin Economic Outlook Autumn 2026.

The global economy is proving remarkably resilient.

High energy prices cloud the outlook but do not stall the global economy

After the outbreak of the Iran war, crude oil prices rose less sharply and for a shorter period than many market participants had initially expected (Figure 5). This is largely attributable to China. In the second quarter of 2026, the country imported an average of 8.1 million barrels of crude oil per day, 32 percent less than in the first quarter. It recorded its lowest imports since 2016. As recently as February, it had been importing around twelve million barrels per day.[5] This decline in demand is likely to have curbed the price increase considerably, although a robust quantification is not yet available. Despite lower oil imports, China's refinery output fell far less sharply than its imports. This was possible because the country holds large strategic oil reserves, which were drawn down substantially in the first half of the year.[6] In addition, the government halted exports of diesel and gasoline in March and capped retail prices in April. The continuing boom in electric vehicles also dampened oil demand.

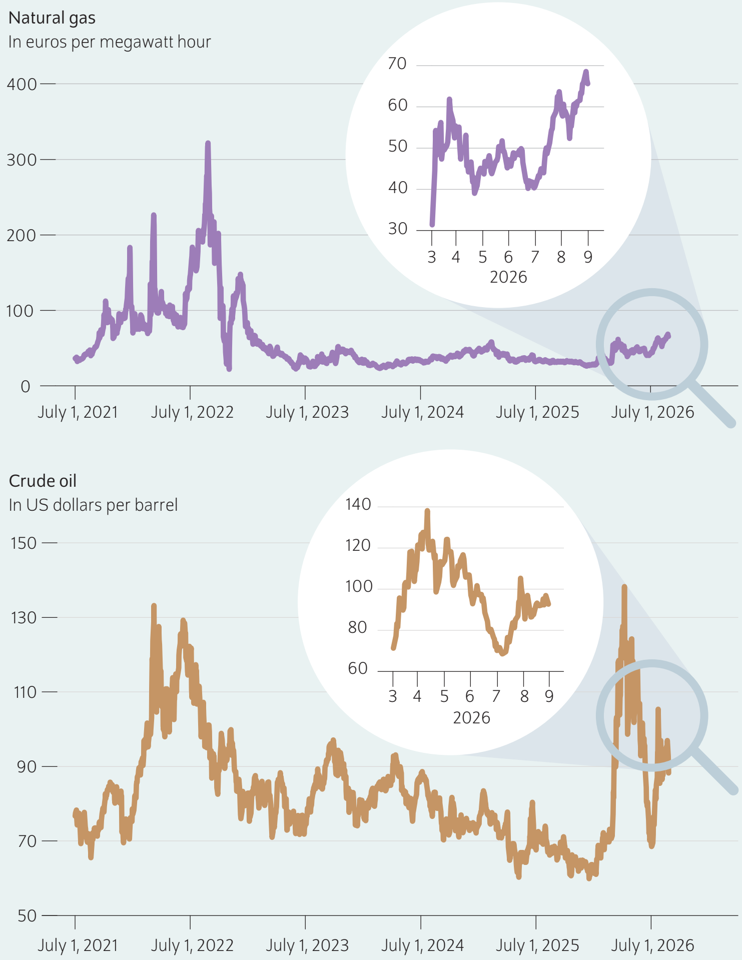
While the price of Brent crude is currently only around 25 US dollars above its pre-war level, prices for refined products such as diesel, gasoline, and kerosene are about 60 US dollars per barrel higher. The refining margin—the difference between the crude oil price and the sales price of the products—has widened by around 35 US dollars per barrel since the war began and reached an all-time high in

5 See U.S. Energy Information Administration (2026): China's Crude Oil Imports Fell in the Second Quarter (available online).

6 How much of the reserves was drawn down remains unclear, as China does not publish inventory data. See Michael Meidan (2026): China's Crude Levers, Oxford Institute for Energy Studies, OIES Energy Comment, May 2026 (available online).

Figure 5

Natural gas and crude oil prices



Note: Last observations: August 25, 2026.

Sources: Intercontinental Exchange (ICE); Energy Information Administration (EIA).

Oil prices responded to the Iran war far more moderately, and the price increase proved shorter-lived, than many had initially expected.

the United States and Europe in July.[7] The reason is that a substantial share of global refining capacity is either blocked inside the Strait of Hormuz or has been knocked out by Ukrainian drone attacks on Russian energy infrastructure. Crude oil that cannot be processed is of little value to buyers. Rationing therefore takes place via product prices. For the economy, this means that the shock has a stronger impact than the crude oil price suggests, because what matters for households and firms are fuel and heating costs, not the price of crude oil. Moreover, the price surge is hitting the transport sector, agriculture, and energy-intensive industry far harder than the rest of the economy. The cost increases in these areas in turn spread broadly across the rest of the economy via value chains. In Europe, the situation is intensifying because gas prices are currently around twice as high as a year ago. All in all, the energy price shock is therefore no larger than assumed in the summer forecast, but its composition has changed: oil prices are below the earlier assumption, gas prices above it.

This forecast is based on the price paths for oil and gas derived from current futures contracts. Compared with the summer forecast, the assumptions for the oil price path have been revised downward and those for the gas price path upward. On an annual average, an oil price of 85 US dollars per barrel is assumed for 2026, 77 US dollars for 2027, and 73 US dollars for 2028. For gas, the assumptions are 50 euros per megawatt hour in 2026, 43 euros in 2027, and 30 euros in 2028. The fact that futures markets expect gas prices to rise further in the coming quarters before declining again mainly reflects the winter effect in European storage management. The euro has recently appreciated against the US dollar and stands at around 1.17 US dollars. This dampens energy costs billed in dollars but at the same time makes European exports more expensive.

The legal basis of US trade policy has shifted again relative to the summer forecast: after the tariffs previously based on Section 122 of the Trade Act expired at the end of July, US tariff collection has since relied on Section 301. The effective average US tariff rate has nonetheless remained almost unchanged compared with the summer forecast. It is assumed that the bilateral US trade agreements—including the one with the European Union—will be continued and that the sectoral tariffs on cars, trucks, steel, and aluminum will remain in force. No new escalation of the tariff conflict is assumed.

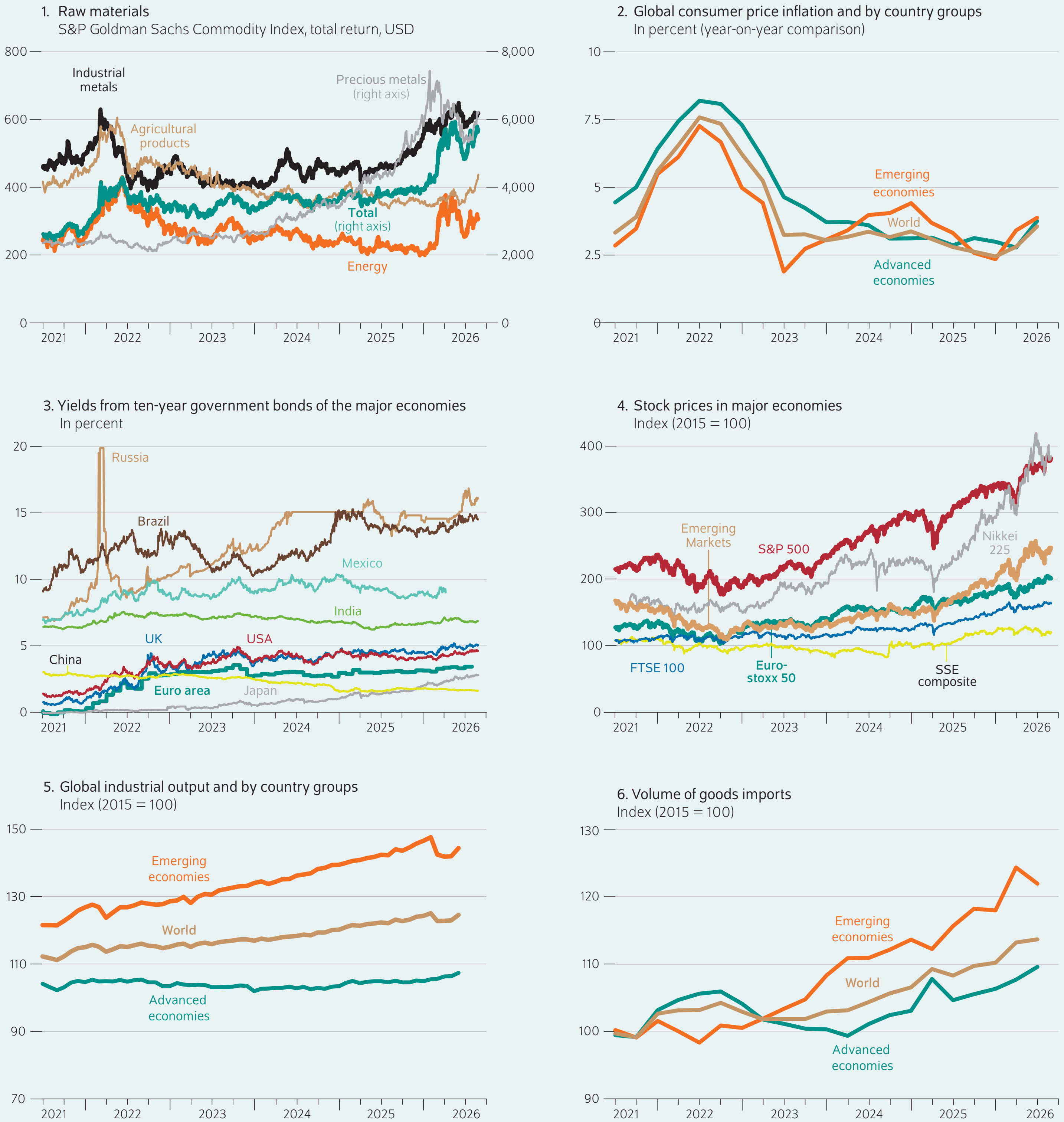
Robust growth expected again this quarter

Despite high energy prices, leading indicators—supported by the ongoing AI investment boom—point to robust growth in the third quarter: both the global purchasing managers' index for manufacturing and the one for services stand at a good 52 points, above the expansion threshold of 50 points. In addition, rising defense spending in many countries is supporting new orders for capital goods. Overall, largely unchanged global growth of 0.8 percent is expected. In the advanced economies, the expansion is likely to hold at 0.4 percent, the level of the two preceding quarters, and in the emerging economies to remain at 1.1 percent, unchanged from the previous quarter. Within the advanced economies, the picture is shifting: in the United States, economic activity is likely to pick up again to 0.6 percent, because the exceptionally strong import momentum of the second quarter is easing and foreign trade is therefore providing support once more. The euro area, by contrast, is likely to merely stagnate in the third quarter, and growth in the United Kingdom is also expected to slow to 0.3 percent. In China, growth is likely to remain stable at 0.9 percent.

7 See International Energy Agency (2026): Oil Market Report—August 2026 (available online).

Figure 6

Indicators of the global economic environment



Notes: Last observations: August 27, 2026 (panel 1); June 30, 2026 (panel 2); August 27, 2026 (euro area: July 31, 2026) (panel 3); August 27, 2026 (panel 4); June 1, 2026 (panel 5); June 30, 2026 (panel 6).

Sources: S&P Dow Jones Indices; Deutsche Börse; CBOE; ECB; PBoC; Federal Reserve; BoE; BOJ; Central Bank of Brazil; Bureau of Labor Statistics; IHS Markit; and CPB World Trade Monitor.

World trade holds course despite the Iran war

World trade continues to prove robust, growing by 0.4 percent in the second quarter compared with the previous quarter (Figure 6). A declining number of global export orders and sharply higher transport costs caused by the Iran war are likely to weigh on world trade. Higher freight rates are taking effect here, driven by higher oil prices and risk premiums. This development continues to be masked, however, by brisk intra-Asian trade, which is driven in part by the global AI boom. In 2026, world trade is still likely to grow by 4.1 percent before weakening to 1.8 percent in 2027. In 2028, it is expected to develop somewhat more dynamically again, at 2.3 percent.

Fiscal policy likely to remain expansionary

Fiscal policy is likely to remain expansionary in most large economies over the forecast horizon. In the United States, the budget deficit is likely to remain high: alongside the tax relief for firms and households under the One Big Beautiful Bill Act, repayments to companies of the IEEPA tariffs ruled unlawful continue to weigh on the government budget. In China, the fiscal stance remains expansionary, but the actual impulses are small and fall short of the announcements. Japan's fiscal policy is also likely to be slightly expansionary overall. Although energy subsidies are being phased out step by step, a temporary reduction in the consumption tax on food from eight to one percent is intended to support consumption from April 2027. For lower and middle incomes, the government will offset the remaining burden through cash payments. The cabinet approved the plan in August, but the legislation still has to be passed at an extraordinary session of parliament planned for the fall. In the euro area, fiscal policy continues to provide slight overall support to the economy, driven above all by Germany. In addition, there are targeted investment support packages in Spain and France. In the United Kingdom, by contrast, the new prime minister, Andy Burnham, has little room for maneuver: the strained state of public finances and the fiscal rules leave hardly any scope for additional fiscal impulses.

Labor market is losing momentum

The labor market in the advanced economies is cooling more noticeably than the still low unemployment rates suggest. In the United States, employment growth over the past twelve months averaged only a good 25,000 people per month, whereas around 235,000 jobs per month were added in the 2022 to 2024 period. This forecast is based on the assumption that AI will have only a moderate effect on the labor market over the forecast horizon. On the one hand, AI effects have so far been concentrated in individual sectors and activities in which hiring was already lower. On the other hand, in many sectors AI is being deployed as a complement to workers rather than as a substitute.

Monetary policy likely to remain slightly restrictive

The energy price shock continues to feed through to consumer prices. While it is initially reflected above all in gasoline prices, slight price increases in further product groups are likely to become visible by mid-2027. In addition to higher energy prices, the loss of fertilizer deliveries is also likely to raise prices and to become noticeable particularly in food prices. Around one third of globally traded urea is shipped through the Strait of Hormuz; the World Bank expects the urea price to rise by around 60 percent in 2026.[8] A further burdening factor is emerging for the coming quarters: an El Niño is building that is likely to be one of the strongest in recent decades and to impair harvests of important staple foods such as rice in Southeast Asia. Alongside energy costs, this weighs above all on lower-income households in the emerging economies, for which food accounts for an above-average share of consumer spending. In the euro area, ETS2—an extension of EU emissions trading—will also be introduced at the beginning of 2028, which is likely to have inflationary effects. Worldwide, the inflation rate is likely to rise from 3.0 percent in 2025 to an annual average of 3.5 percent in 2026 and to fall back to 2.7 percent in 2027. In 2028, it is likely to stand at 2.6 percent.

Against this background, monetary policy is likely to remain slightly restrictive over the forecast horizon. It is assumed that the European Central Bank (ECB) will raise rates by a further 25 basis points to a deposit rate of 2.5 percent at its next Governing Council meeting. A first rate cut is not assumed until the first quarter of 2028. In the United States, the Federal Reserve under its chairman Kevin Warsh is likely to raise rates by 25 basis points in September and then to wait. The Bank of England has ended its cutting cycle and is likely to keep its policy rate constant. The Bank of Japan recently raised its policy rate to 1.0 percent, the highest level in over 30 years. The yen had previously fallen to a 40-year low. At the beginning of August, Japan and the United States intervened jointly in the foreign exchange market for the first time since 2011; the yen has since been trading at around 155 to the US dollar.

Global economy to grow by a good three percent in 2026 and 2027

The global economy is likely to continue expanding moderately over the forecast horizon through the end of 2028. While rising military spending in many countries, a slightly expansionary fiscal policy, and the AI boom are supporting demand, high energy prices are weighing on economic momentum. In the United States, economic activity remains largely driven by the ongoing AI investment boom, particularly through investment in equipment and intellectual property. In private consumption, higher energy prices are eroding purchasing power. Moreover, while the tax relief under the One Big Beautiful Bill Act continues to support disposable

8 See World Bank (2026): Fertilizer Prices Surge as Strait of Hormuz Disruptions Tighten Supplies. World Bank Data Blog (available online).

Table 6

Real gross domestic product, consumer prices, and unemployment rate in the global economy
In percent

	GDP				Consumer prices				Unemployment rate in percent			
	Year-on-year percentage change											
	2025	2026	2027	2028	2025	2026	2027	2028	2025	2026	2027	2028
Europe												
European Union	1.5	1.2	1.5	1.6	2.5	3.0	2.7	2.7	6.0	6.0	6.1	6.0
Euro area	1.3	0.9	1.2	1.2	2.1	2.8	2.2	2.3	6.4	6.4	6.3	6.2
... excluding Germany	1.9	0.8	1.3	1.2	2.0	2.8	2.8	2.1	7.4	7.4	7.3	7.1
France	0.9	0.5	0.7	0.9	0.9	2.3	2.3	1.2	7.7	8.2	8.0	7.7
Italy	0.7	0.9	0.6	0.5	1.6	2.8	2.6	1.8	6.0	5.7	6.0	6.2
Spain	2.8	2.7	2.0	1.9	2.7	3.4	3.0	2.1	10.5	10.2	9.8	9.5
Netherlands	1.6	1.4	1.0	1.2	3.0	2.7	2.5	2.1	3.9	3.8	3.6	3.6
United Kingdom	1.3	1.2	1.4	1.7	3.4	3.2	2.7	2.0	4.9	5.0	4.8	4.8
Switzerland	1.4	1.2	1.6	1.5	0.2	0.7	0.7	0.8	4.3	4.7	4.6	4.4
Central and Southeastern Europe	2.5	2.4	2.7	2.7	4.3	4.2	4.3	3.8	4.0	4.0	4.0	3.9
Turkey	3.6	3.4	4.1	4.6	34.9	30.3	24.9	15.1	8.4	8.4	8.3	8.0
Russia[1]	1.1	0.4	1.5	1.8	8.7	6.9	5.3	4.3	2.2	2.3	2.5	2.4
The Americas												
USA	2.1	2.1	1.9	2.2	2.7	3.2	1.9	1.8	4.3	4.2	4.5	4.7
Mexico	0.8	1.5	2.3	2.0	3.8	3.5	3.0	3.0	2.6	2.9	2.8	3.0
Brazil	2.6	2.2	2.1	2.1	5.0	5.2	4.8	3.2	6.0	5.9	6.2	6.5
Asia												
Japan	1.2	0.7	0.7	0.8	3.2	2.2	2.3	1.8	2.5	2.5	2.5	2.5
South Korea	1.1	3.2	1.8	2.0	2.1	2.9	2.2	2.8	2.8	2.9	2.9	2.9
China	5.0	4.4	4.3	4.3	−0.2	1.1	0.7	1.2	5.2	5.2	5.1	5.1
India	7.3	6.9	6.5	6.4	2.2	4.6	4.1	4.0	7.2	6.8	6.4	6.2
Total												
Advanced economies	1.7	1.6	1.6	1.8	3.0	3.2	2.2	2.1	4.6	4.6	4.7	4.7
Emerging economies	5.1	4.7	4.7	4.8	3.0	3.8	3.2	3.0	5.7	5.6	5.4	5.4
Global economy	3.5	3.2	3.2	3.4	3.0	3.5	2.7	2.6	5.4	5.4	5.3	5.3
For reference:												
Export weighted[2]	2.2	2.1	2.0	2.2								
GDP weighted in USD[3]	2.9	2.7	2.7	2.9								

1 The data forecast for Russia are subject to considerable uncertainty. Russia has only a small weight in the overall forecast.
2 World weighting based on shares of German exports in 2024.
3 World weighting based on gross domestic product in US dollars from 2024 to 2027.

Notes: The black figures represent actual (reported) data. The values for country groups are weighted averages. For weighting real GDP and consumer prices, the respective GDP in purchasing power parities from the IMF World Economic Outlook for the years 2024 to 2027 is used. For weighting unemployment figures in the country groups, the labor force (ages 15 to 64) of each country for the year 2023 is used. The Central and Southeastern European countries include Poland, Romania, the Czech Republic, and Hungary.

Sources: National statistical offices; DIW Berlin Economic Outlook Autumn 2026.

income, it no longer provides an additional growth impulse. At the same time, declining real wages and an already low saving rate leave hardly any buffer for consumption; it is increasingly being carried by high-income households. Overall, the US economy is likely to grow by 2.1 percent this year, 1.9 percent in 2027, and 2.2 percent in 2028. The unemployment rate is likely to rise from 4.2 percent in 2026 to 4.7 percent in 2028. In the euro area, growth is increasingly being driven by domestic demand, while foreign trade provides hardly any impulses: weak price competitiveness, US tariffs, and the strong euro are weighing on exports. Expansionary fiscal policy is providing support, driven by public investment in infrastructure and defense. The stable labor market additionally supports consumption, although households' purchasing power is likely to be slightly constrained by increased transport and heating costs. Overall, the euro area economy is likely to grow by 0.9 percent this year. In 2027 and 2028, growth of 1.2 percent in each year points to an acceleration. This represents a revision of plus 0.6 and 0.3 percentage points, respectively, compared with the summer forecast, which is mainly due to Germany's surprisingly strong momentum. The unemployment rate is likely to decline from 6.4 percent in 2026 to 6.2 percent in 2028.

In China, domestic economic activity is likely to remain subdued: the ongoing real estate crisis and the high indebtedness of households and local governments are weighing on investment and private consumption. Growth is instead being driven by exports, particularly of technology goods. The Chinese economy is likely to grow by 4.4 percent this year and by around 4.3 percent in each of the two following years, thus remaining somewhat below the government's target range of 4.5 to 5.0 percent.

Overall, the global economy is likely to grow by 3.2 percent this year and next. For 2028, an increase of 3.4 percent is expected (Table 6). For the advanced economies, growth of 1.6 percent is projected for 2026 and 2027 and of 1.8 percent for 2028; for the emerging economies, around 4.7 percent in each year. Compared with the summer forecast, the projection for the global economy is thus somewhat higher for 2026 (plus 0.1 percentage points) and slightly lower for 2027 (minus 0.1 percentage points).

Escalation of the Iran war and weaker AI investment are the greatest risks

The outlook remains subject to considerable risks. The main downside risk continues to stem from an escalation of the Iran war. A prolonged blockade of the Strait of Hormuz and further attacks on refining capacity would raise energy prices more sharply and more persistently than assumed. Scenarios of up to 120 US dollars per barrel cannot be ruled out. In this case, the negative energy contributions to inflation in 2027 would fail to materialize and the inflation rate would not decline further as assumed. A prolonged blockade would at the same time extend the loss of fertilizer deliveries through the Strait of Hormuz. This would drive food prices up further—on top of the strong El Niño effect already assumed in the forecast. The oil price risk would increase further if China were to expand its crude oil imports again, for instance because its reserves are running low. An additional demand impulse would then meet supply that remains throttled.

A second risk lies in the AI boom itself. Since it supports economic activity in this forecast, a correction would have far-reaching consequences: a slump in AI-related investment would hit not only the United States but, via semiconductor supply chains, also Southeast Asia directly.

A third risk concerns the labor market. The forecast assumes that AI will predominantly be deployed as a complement to workers. Should AI prove to be more of a substitute than a complement across the board, unemployment would be likely to rise more strongly over the forecast horizon than expected here. This would dampen wage momentum and, through weaker private consumption, weigh on overall economic developments.

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