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Talking point

German industry: Only marginal increase in output at start of 2015

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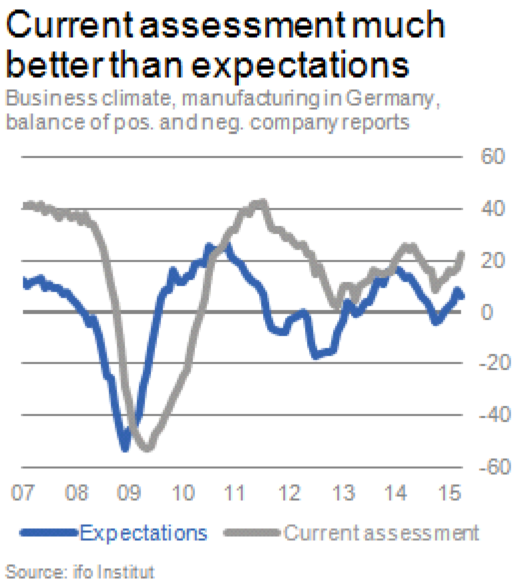
Despite only marginally higher output in Germany's manufacturing sector in Q1 2015 we are sticking with our full-year production forecast (+1.5% in real terms). The current softness of the euro benefits Germany's export sectors. Nonetheless, companies appear much more upbeat in their assessment of the current situation than in their expectations for the coming months. This is likely due, for example, to continuing geopolitical risks and poorer economic policy conditions in Germany. So it is clear that in the business world not everything is sweetness and light.

The real production index for the manufacturing sector in Germany was only up by a seasonally adjusted 0.1% in Q1 2015 on the Q4 2014 value. This was the second quarterly increase in a row. The reading for the start of the year roughly dovetails with our output forecast for 2015 as a whole (1.5% in real terms), which we reassert at this juncture. We expect moderate output growth in each of the coming quarters as the year progresses. As such, it would fall short of the average (annual) increase since 2000 of 2%.



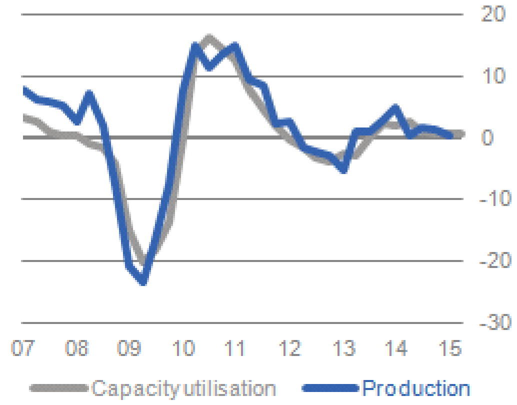
The economic environment for German industry is generally quite favourable at present. Export-intensive sectors are benefiting from the euro's slide and relatively robust growth figures in key markets such as the US. There, the expected slight decline in GDP in Q1 that was driven by one-off factors should remain a temporary phenomenon. The eurozone's recovery is continuing apace, even though its momentum remains only moderate. Growth has slowed in China compared to past years, but all in all the effects should be manageable, especially considering that the absolute growth of economic output in China remains remarkably high and (based on purchasing power parities) is equal to the GDP of Poland and Portugal combined. Low prices for oil and other commodities are providing cost relief in Germany. Of course, still low interest rates are also continuing to do their share. Private consumption is growing strongly in Germany – thanks not least to good labour market performance, relatively high wage settlements and lower mobility and energy costs.

Nevertheless, not all indicators point to a "smooth" upswing in Germany's industrial sector. In Q1, for instance, manufacturing orders were 1.6% lower in real terms than in the preceding quarter. Order intake has been very volatile over the past few months anyway, due partly to the relatively large fluctuations in the volume of big-ticket orders. Still: there has not yet been any sign of a clear uptrend in order activity in the recent past.

It fits the picture that capacity utilisation in the manufacturing sector is down slightly at the beginning of Q2, albeit at a relatively high level. Even business expectations have fallen slightly of late, and are now only barely in positive territory. By contrast, manufacturers are much more upbeat on their current situation. It appears as if company managers in Germany think the situation is "too good to last", which is why there are no signs of euphoria emerging despite the favourable environment discussed above – such as the softness of the euro in particular. And several factors are indeed weighing on business sentiment. The regional political and/or military conflicts in Europe and on Europe's doorstep have not yet been solved (e.g. conflict in eastern Ukraine, Islamic State terrorism and civil war in the Middle East). World trade is growing only sluggishly by long-term standards. Given the lower oil prices, many oil-exporting countries will probably import fewer goods from Germany in 2015 than in 2014. Within the eurozone the "Greece issue" remains firmly on the agenda. Furthermore, many German companies are probably sceptical about the unconventional monetary policy of the European Central Bank – benchmarked against traditional Bundesbank policy of earlier days. On top of this, the economic policy environment for corporates in Germany has tended to become increasingly cloudy in recent months, or at least has not improved appreciably (e.g. pension, labour market and energy policies). And, finally, the higher wage settlements also mean higher costs for companies. Whether these factors will actually manifest themselves as temporary burdens on companies remains to be seen. It is clear, however, that in the business world not everything is sweetness and light. On balance, in view of this mixed picture we still feel comfortable about leaving our industrial output forecast unchanged for now.

Only little momentum

Capacity utilisation and production, manufacturing in Germany, quarterly values, % yoy



Sources: ifo Institut, Federal Statistical Office

Even considering the situation in the major manufacturing sectors we still see no need after the Q1 results to tweak our production forecast for the full year. True, mechanical engineering started the new year on a poorer note than expected. And electrical engineering has tended to surprise on the positive side. All in all, though, we believe our current assessments are still plausible. We expect the automotive industry and mechanical engineering to each grow their output by 2% in real terms. Electrical engineering, chemicals and the metals industry as a whole are poised for growth of 1.5%. Note, interestingly, that the production data for the chemicals industry have been significantly revised retroactively (as expected), which is why 2014 now shows a decrease of only 1.3% (previously -2.9%). We look for the food industry to post growth of 0.5% in 2015.

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Read more: Heymann, Eric (2015). How is the weak euro affecting different sectors? Who is benefiting and who is losing out? Deutsche Bank Research.Current Issue. Frankfurt am Main.

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