

## Talking point

### Germany's manufacturing output disappoints at the end of 2015 and starts 2016 with a burden

February 22, 2016

**Manufacturing output in Germany increased by 1.1% in real terms in 2015. Just over half of this growth resulted from 2015 having more working days than 2014. Among the main industrial sectors, pharmaceuticals (+4.3%) and automotives (+2.6%) recorded the highest growth rates. By contrast, the mechanical engineering and chemical industries suffered declines in production of 1.1% and 0.4% respectively. Mixed signals are currently shaping the outlook for 2016. For example, the slowdown in growth in major sales markets is being offset by a relatively high capacity utilisation rate in industry at the start of the year, as well as a positive trend in core orders. On the whole, we confirm our forecast that manufacturing output in Germany is not likely to do more than stagnate in 2016. Nevertheless, in light of global economic and geopolitical risks, as well as turmoil in the financial and commodities markets, a certain disturbing feeling remains to the effect that manufacturing output in Germany could also be worse than projected this year.**

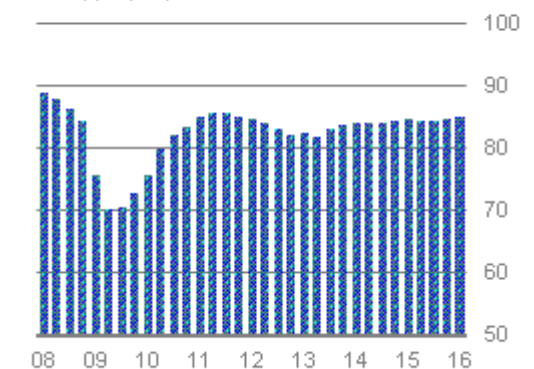
In real terms, German manufacturing output in the fourth quarter of 2015 was down by a seasonally adjusted 0.9% on the preceding quarter. This was the second consecutive quarterly decline and the strongest since the fourth quarter of 2012. It is only thanks to a relatively positive performance in the first half of 2015 that the sector increased its domestic production by 1.1% in real terms in the full year. However, this resulted in the growth rate declining by half compared to 2014. In addition, the momentum was lower than for GDP in Germany, which expanded by 1.7% in real terms in 2015. Regarding the annual result in the manufacturing industry, it is interesting to note that on a working-day adjusted basis, domestic production rose by only 0.4% in 2015. Accordingly, more than half of the growth recorded in 2015 is attributable to the fact that the year had an additional two working days compared to 2014. Although new manufacturing orders in the fourth quarter of 2015 rose by an inflation-adjusted 1% on the previous quarter, this was not enough to offset the major setbacks incurred in the third quarter (-2.7% on the preceding quarter). Consequently, on the whole, German industry recorded a disappointing performance at the end of 2015.

Among the main industrial sectors, in 2015 it was the pharmaceutical industry that made the highest production gains, increasing by 4.3%. The automotive industry also achieved above-average growth of +2.6%, although the sector reported a marked downward trend in the fourth quarter. Both the pharmaceutical and the automotive industries benefited, among other things, from strong momentum in foreign trade, whereby the depreciation of the euro in relation to the currencies of key trading partners had a favourable effect. Individual sub-sectors of the plastics industry benefited from positive consumer spending in Germany, with production growing by 2.4% in 2015. Electrical engineering achieved a plus of 1.2%, while the metal industry was up 0.8%. By contrast, mechanical engineering and chemicals (excluding pharmaceuticals) suffered production declines of 1.1% and 0.4% respectively. While a favourable euro-US dollar exchange rate spurred mechanical engineering exports to the US, a decline in exports to China and Russia, among other things, had a dampening effect on domestic production. In the chemical industry, the slight downtrend in production from end-2013 continued, although at least new orders edged upwards in the second half of 2015.

#### Outlook 2016: Mixed signals and statistical burden

#### Capacities well utilised

Capacity utilisation in the manufacturing industry, sa, DE, %



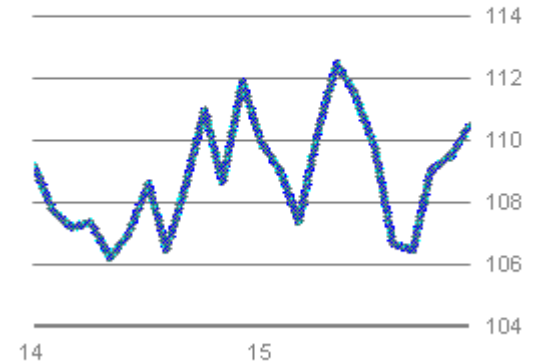
Source: ifo Institut



The outlook for 2016 is currently marked by mixed signals. We recently revised our forecast for global GDP growth slightly downwards to 3.1% in 2016. On the whole, stimuli from abroad for export-oriented German industry are likely to be weaker in 2016 than in 2015, especially in light of the stronger-than-expected euro at the start of the year. Although the low oil price should favour private consumption in many oil-importing countries, this will be offset by declining investment levels not only, but primarily, in the oil-producing countries. Given that the focus of German industry is on capital goods, the negative impact of a very low oil price on exports to non-European countries could even predominate; in this connection, there are added concerns regarding the macroeconomic stability of countries whose national budgets rely strongly on oil and gas exports. In any event, there is no shortage of economic and geopolitical risks worldwide. In view of the negative signals, it is hardly surprising that manufacturers' business expectations have now fallen significantly. While these are still just within positive territory, they do not take into account the most recent share price losses and other negative reports. A statistical burden exists for the manufacturing industry given that domestic production will have started the new year with a noticeable underhang. Of course, it remains to be seen if this might be eased by revisions in the next production figures (above all, those for December). One indication is that real industry turnover figures were recently better than those for output.

## Core orders recently on an upward trend

New manufacturing orders, excl. other transport equipment, sa, DE, 2010=100



Source: Federal Statistical Office

Apart from a relatively stable turnover development, capacity utilisation is another positive signal coming from the manufacturing industry. This rose at the beginning of the first quarter of 2016 to over 85% and, consequently, its highest level since the end of 2011. Further confidence can be derived from the fact that German industry's core orders – i.e. orders excluding volatile large orders in the manufacture of other transport equipment (aircraft, ships) – trended upwards in the second half of 2015. It is also an advantage for German industry that economic recovery in the European Union is likely to continue in 2016, albeit slowly and despite our recent forecast revision for GDP growth in the euro area from 1.6% to 1.4%. This could still make up for falling export levels in other countries. Ultimately, monetary policy in the euro zone should also remain expansionary in 2016, although it should be taken into account that, thus far, the long phase of low interest rates has only been a minor incentive for companies in Europe to increase their investments.

### A break-even figure in production likely

In conclusion, we confirm our forecast that manufacturing output in Germany is not likely to do more than stagnate in 2016. Also, in the main industrial sectors, i.e. automotives, mechanical and electrical engineering, chemicals, metals and food, the rate of change in domestic production could be close to 0%. At least the current data situation does not suggest that major outliers are to be expected. Given the statistical underhang which is especially pronounced in the automotive and mechanical engineering industries, production will, on the whole, have to trend upwards in the course of 2016 in order to even reach our expectation of a break-even figure.

If our projection of – at most – marginal growth in manufacturing output in 2016 were to prove correct, it would mean a continuation of the current phase of relatively minor economic movements and overall sluggish momentum that began in 2012. Nevertheless, in light of global economic and geopolitical risks, as well as turmoil in the financial and commodities markets, a certain disturbing feeling remains to the effect that manufacturing output in Germany could also be worse than projected this year.

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