BDI
The Voice of German Industry

QUARTERLY REPORT GERMANY

Industry anticipating 1.8 percent rise in GDP.

Global upturn is the main factor

Quarter III / 2017

- **The German economy is picking up speed considerably.** We are expecting real economic output to increase by **1.8 percent** this year compared to 2016. After calendar adjustment, that corresponds to growth of slightly over two percent.

- **In the first half of the year, the German economy grew by just over two percent year on year.** GDP growth in the second quarter, following price, calendar and seasonal adjustment, was 0.6 percent over the previous quarter following growth of 0.7 percent in the first quarter.

- **Exports surpassed expectations by climbing just under four percent in the first six months of the year.** We are expecting exports to maintain this pace of growth in the second half of the year.

- **Investment activity developing in line with our estimates.** Investment in construction is set to rise along with capital investment in plant and equipment given the high levels of industrial capacity utilisation.

- **The main driver of German economic growth in the second half of the year is likely to be private consumption.** This is buoyed by a continued rise in jobs subject to social security contributions.

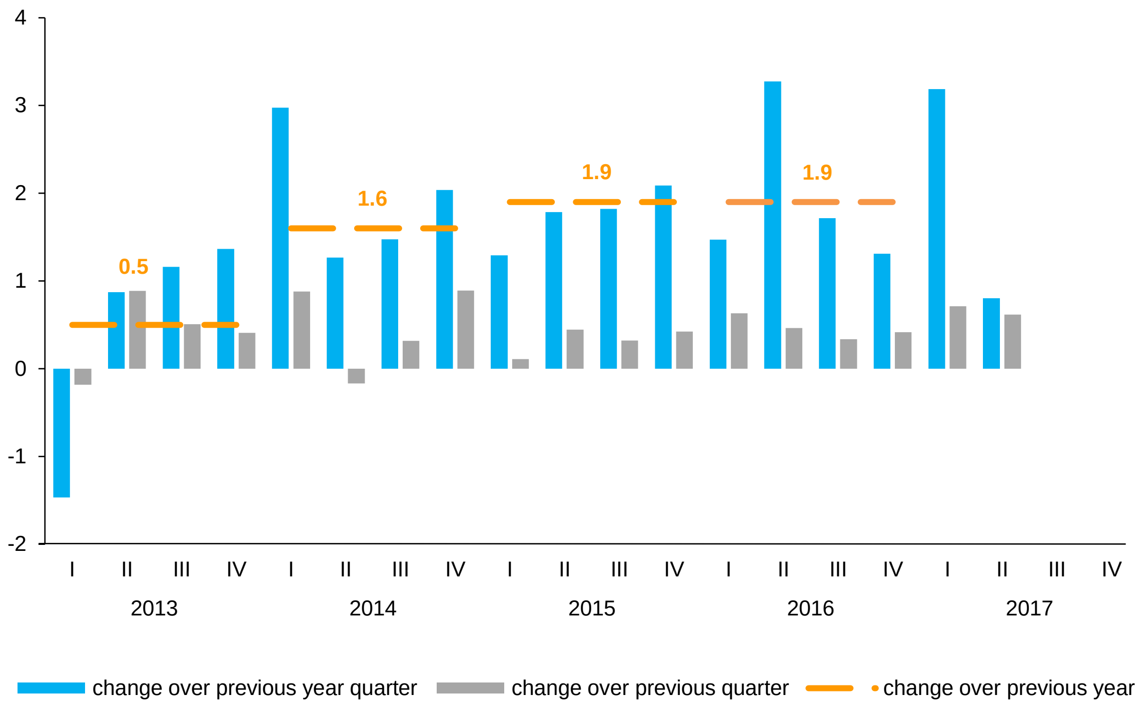
Content

The German economy

Strong GDP growth in the first half of 2017

The German economy got off to a good start this year, growing solidly. In the second quarter of 2017, Germany's gross domestic product increased by 0.6 percent over the previous quarter after price, calendar and seasonal adjustment, following growth of 0.7 percent in the first quarter of 2017 and 0.4 percent in the fourth quarter 2016. Compared to last year, second quarter economic output was up by 0.8 percent following price adjustment. After calendar adjustment, which was unusually pronounced with three more working days in the first quarter and three fewer working days in the second quarter, GDP grew by 2.1 percent after growing two percent in the first quarter.

Growth in real GDP in percent



Source: Federal Statistical Office

In the second quarter 2017, the economic output was generated by a workforce of 44.2 million people. That is 644,000 or 1.5 percent more people than in the same period last year. The number of jobs increased in all economic sectors apart from agriculture and forestry, and financial and insurance services. Sectors that registered the biggest increases in jobs were public services, education and healthcare (up 224,000), corporate services (up 153,000) and trade, transport and hospitality (up 130,000). The rise in employment in manufacturing was much more moderate, with only 50,000 more jobs. Gross value added grew most in the information and communication sector, going up 3.7 percent over the same period last year. The construction sector also experienced growth, although gross value added here only went up by 1.5 percent. The minor decrease in value added in manufacturing and production is likely due to the high levels of value added in the same period last year. The number of working days also has a greater impact on these sectors than it does on services.

On the expenditure side of GDP, momentum came particularly from the domestic economy. **Household consumption expenditure** increased by 0.8 percent over the previous quarter after price, seasonal and calendar adjustment, following an increase of 0.4 percent in the first quarter. The public sector consumption was also a significant 0.6 percent more than in the previous quarter. Consumption overall contributed 0.6 percentage points to growth. **Gross fixed capital formation** increased by one percent. **Capital expenditure on plant and equipment** (up 1.2 percent), **construction investment** and **investment in other assets** (each up by 0.9 percent) all increased substantially over the previous quarter. In sum, gross fixed capital formation made a positive contribution to growth of 0.4 percentage points, including 0.2 percentage points of growth on account of changes in inventories. Domestic consumption, overall, contributed one percentage point to growth. In a turnaround to the start of the year, **net exports** did not contribute to GDP growth. Imports outpaced exports by far in the second quarter, pulling down growth overall by 0.3 percentage points.

Foreign trade: second quarter sees slight rise in exports set against robust rise in imports

In the second quarter 2017, **exports** rose by 11.6 billion euros or 3.8 percent year on year, totalling 319 billion euros (country-specific seasonally adjusted data not available). As in the first quarter 2017, the largest nominal increases in exports were those to China, which increased by 1.49 billion euros or 19.6 percent. Exports to neighbouring countries also performed well: the Netherlands (up 1.40 billion euros or 7.1 percent), Switzerland (up 1.35 billion euros or 10.8 percent), France (up 1.26 billion euros or 4.9 percent) and Poland (up 1.05 billion euros or 7.9 percent). Exports to Russia made a remarkable recovery with exports rising by 21 percent or 1.11 billion euros, making the country the fourth biggest destination for exports outside the European Union. Despite the British pound depreciating by almost nine percent, exports to the United Kingdom only dropped by 833 million euros or 3.8 percent. Exports to Turkey were down by 716 million euros or 11.8 percent. Exports to Algeria, which had plunged down more than 50 percent in the first quarter 2017, almost doubled in the second quarter, surging back with an increase of 773 million euros. Trade with the Gulf states suffered major drops, with exports to Saudi Arabia falling by 353 million euros or 18.9 percent and exports to the United Arabic Emirates tumbling 1.64 billion euros or 40.2 percent.

The strong increase in **imports** already registered in the first quarter continued into the second quarter 2017. Year on year, imports increased by 19.65 billion euros or 8.3 percent to reach 256.6 billion euros. The biggest nominal increases by far were imports from China (up 2.69 billion euros or 12.5 percent). Apart from the Netherlands, where imports to Germany registered the second largest increase, imports from countries outside the EU increased especially. Imports from Russia, which increased by 1.65 billion euros or 27.1 percent, were up in part due to the increased prices of energy commodities as with imports from Norway. Imports from the US rose by 1.17 billion euros or 8.2 percent. South Korea's exports to Germany increased by 59.7 percent or 1.14 billion euros. Higher-than-average growth in imports was also recorded from: Mexico (up 593 million euros or 46.5 percent), South Africa (up 351 million euros or 22.2 percent) and Malaysia (up 342 million euros or 18.7 percent). Imports from France also trended unusually, decreasing in the second quarter by 1.50 billion euros or 8.7 percent. In absolute terms, exports from France to Germany were down by twice as much as the drop in exports to Germany from all other countries taken together. The main reason for this drop is that considerably fewer airplanes were imported from France in the reporting period than in the same period last year.

Development of exports and imports in selected countries in Q2 2017
Year-on-year change

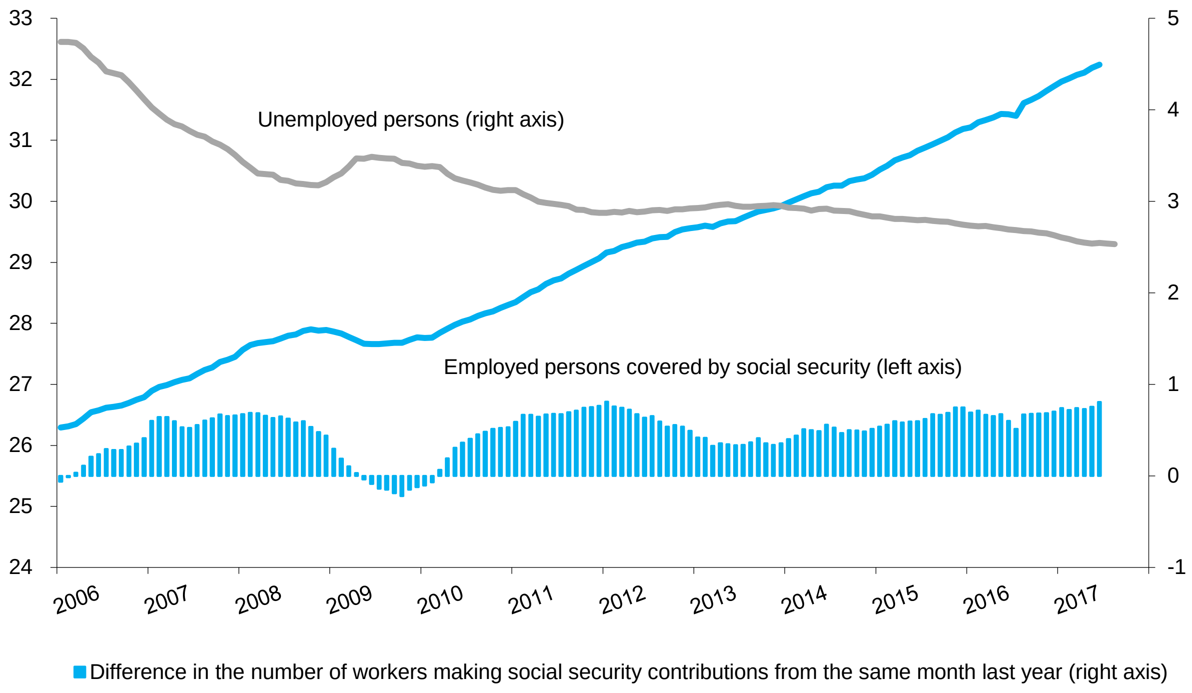
increase (+) or decrease (-) in exports					increase (+) or decrease (-) in imports				
Destination	in million euros		in %		Origin	in million euros		in %	
China	20 661	+ 1 492	+	7.8	China	24 132	+ 2 689	+	12.5
Netherlands	21 098	+ 1 402	+	7.1	Netherlands	22 369	+ 1 788	+	8.7
Switzerland	13 851	+ 1 346	+	10.8	Russia	7 727	+ 1 650	+	27.1
France	27 045	+ 1 260	+	4.9	USA	15 458	+ 1 174	+	8.2
Russia	6 424	+ 1 113	+	21.0	South Korea	3 044	+ 1 137	+	59.7
Poland	14 801	+ 1 047	+	7.6	Czech Republic	11 718	+ 931	+	8.6
Italy	16 672	+ 810	+	5.1	Poland	12 415	+ 913	+	7.9
Czech Republic	10 681	+ 779	+	7.9	Italy	14 135	+ 898	+	6.8
Algeria	1 445	+ 773	+	114.9	Spain	8 028	+ 753	+	10.3
Austria	15 799	+ 672	+	4.4	Norway	3 491	+ 689	+	24.6
Belgium	11 398	+ 600	+	5.6	Mexico	1 867	+ 593	+	46.5
Mexico	3 249	+ 517	+	18.9	Romania	3 590	+ 528	+	17.2
Finland	2 784	+ 419	+	17.7	Belgium	10 563	+ 490	+	4.9
Hungary	6 349	+ 372	+	6.2	Austria	10 175	+ 480	+	4.9
					Switzerland	11 173	+ 401	+	3.7
Saudi Arabia	1 518	- 353	-	18.9	South Africa	1 933	+ 351	+	22.2
Cayman Islands	110	- 452	-	80.5	Malaysia	2 173	+ 342	+	18.7
Turkey	5 352	- 716	-	11.8	Libya	416	+ 334	+	406.4
UK	21 050	- 833	-	3.8					
U. A. Emirates	2 444	- 1 642	-	40.2	France	15 765	- 1 497	-	8.7
Total	**319 044**	**+ 11 591**	**+**	**3.8**	**Total**	**256 583**	**+ 19 648**	**+**	**8.3**

Sources: Federal Statistical Office, own calculations

Labour market: employment continues rising throughout summer

According to preliminary data from the German Federal Statistical Office, the number of **employed** rose to 44.39 million individuals in August 2017. That means around 700,000 more people (or 1.6 percent) had a job than at the same time last year. The increase in jobs was largely due to an increase in the number of jobs **subject to social security contributions**. According to the latest projections by the German Federal Employment Agency, in June 2017 (latest available data) a total of 32.18 million people were in employment subject to social security contributions. This represents an increase of 809,000 people or 2.6 percent compared with one year ago.

German labour market*



*seasonally adjusted in million

Source: Federal Employment Agency

It should be noted, however, that these figures are likely to be slightly exaggerated due to data processing errors last year. The number of **self-employed** including contributing family workers dropped in the second quarter 2017 by 26,000 or 0.6 percent to 4.33 million. The number of **people exclusively in marginal employment** dropped in June 2017 by 87,000 or 1.7 percent down to 4.78 million, according to preliminary figures from the Federal Employment Agency. Unemployment decreased in the new German states in particular. The number of people registered as unemployed in August 2017 dropped down to 2.545 million. That is 139,000 individuals or 6.4 percent less than the same time last year. In August 2017 the **unemployment rate** as calculated by the Federal Employment Agency was at 5.7 percent, or 3.9 percent according to the ILO calculation.

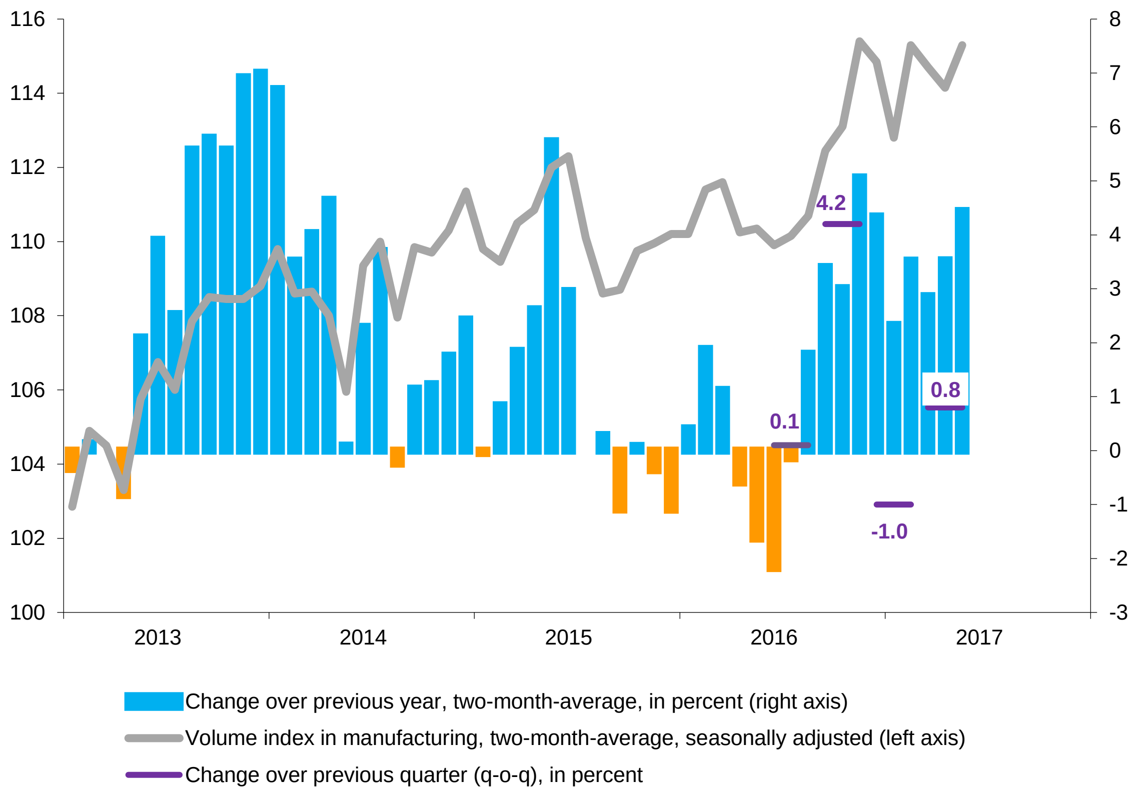
Industry

Order books in industry growing, with growth expected to continue at moderate pace

In June 2017 the **order intake** for German industry increased by one percent over the previous month according to preliminary data and following price, calendar and seasonal adjustment. In May, incoming orders even increased by 1.1 percent after a slight upward revision. Excluding large orders, the order intake in June would have increased by two percent. Domestic demand increased by 5.1 percent compared to May 2017. Orders from abroad, in contrast, dropped by two percent. Demand from the euro area fell by 2.4 percent. Countries outside the euro area ordered 1.5 percent less industrial goods.

The less volatile **two-month comparison** shows an increase in orders of 0.6 percent between May/June 2017 and March/April. Compared to the same period last year, new orders increased for the tenth time in a row, this time by 4.5 percent. The latest figures show an increase in domestic orders of 2.8 percent, with orders from abroad up 5.7 percent. Demand for industrial goods from within the euro area has increased since the start of the year.

New orders, manufacturing



Source: Federal Statistical Office

Among the main groups of industrial goods, producers of **intermediate goods** received 1.3 percent more orders in May/June 2017 than in March/April. Demand from abroad for **intermediate goods** increased by 2.3 percent, with domestic orders only increasing by 0.4 percent. The latest figures show a robust year on year increase of 6.1 percent.

The demand for **capital goods** increased by 0.5 percent in the two-month comparison between May/June 2017 and March/April. Domestic demand for capital goods increased by 0.7 percent. Foreign demand for capital goods increased by 0.3 percent. Year on year, demand for capital goods was up 3.4 percent.

Consumer goods producers recorded a decrease in orders between May/June 2017 and March/April of two percent. Although domestic demand increased for the third consecutive time, going up by a sturdy 2.6 percent, orders from abroad decreased by five percent after pointing up for the last three months. The increase year on year was a hefty 4.7 percent.

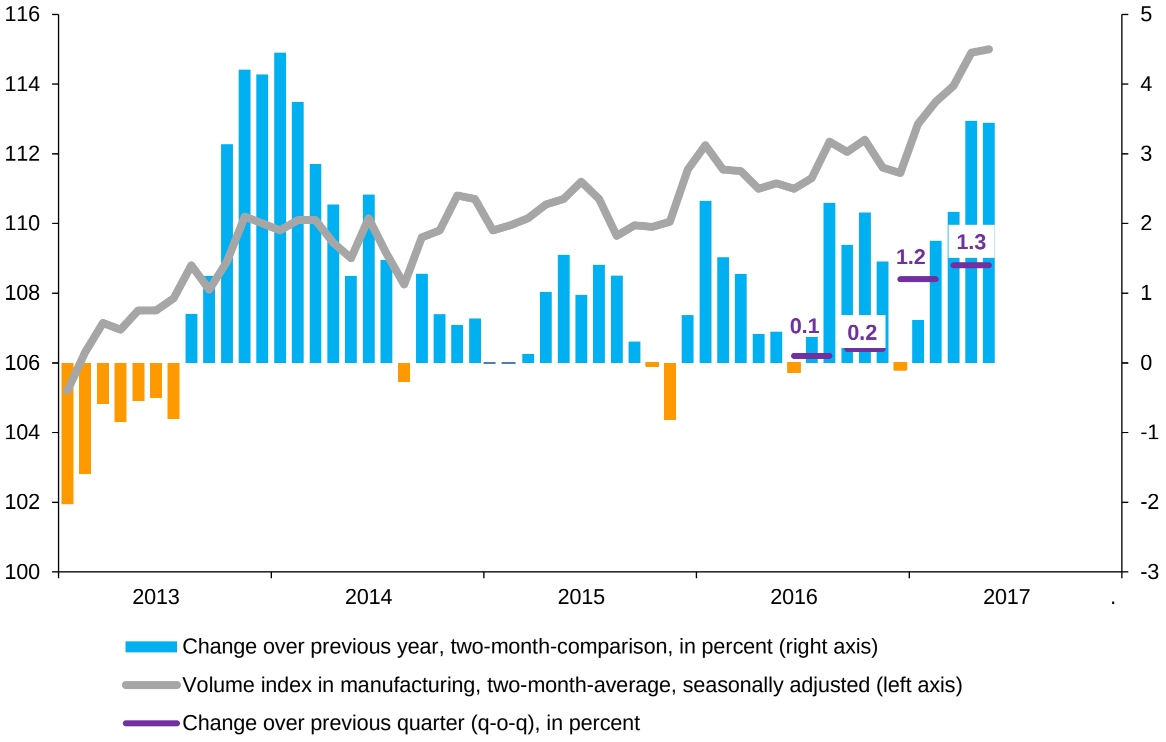
The order books of German industry have improved substantially in the second quarter 2017. New orders have piled in, particularly from the euro area, with orders registering high single-digit growth in the last three quarters. Among the main industrial groups, demand increased particularly for intermediate and consumption goods, which should be reflected in correspondingly higher production levels in the coming months. The somewhat more volatile demand for capital goods increased for the fourth successive time, but appears to be losing steam slightly according to the latest figures. Overall, the positive trend in incoming orders should keep manufacturing output buoyant.

Sturdy expansion of production in second quarter though latest figures show slight tail-off

In June 2017, the output of the **production industries** nudged down 1.1 percent compared to May 2017 following price, calendar and seasonal adjustment, according to preliminary data. This was the first decrease in output in this sector in five months. While **energy production** increased by 1.4 percent in June, production in the **construction sector** was down by one percent. Industrial output decreased by 1.4 percent compared to the previous month, with all main industrial groups registering negative growth. The producers of capital goods cut their production by 1.9 percent, intermediate goods production decreased by 1.2 percent and production of consumer goods by 0.7 percent.

Despite the drops in production, the underlying trend remains positive particularly given that the production data for May was exceptionally good. The less volatile **two-month comparison** shows an increase of one percent for the production industries, with an increase of 3.6 percent year on year. The **construction sector** even managed a year-on-year increase of five percent despite the slight decrease registered in the latest figures. **Industrial output** increased by 0.7 percent between May/June 2017 and March/April 2017. Year on year, the increase in industrial output was considerably higher at 3.3 percent. Among the **main industrial groups,** consumer goods producers recorded an increase of one percent compared to the previous period. The production of capital goods rose by 1.5 percent. Intermediate goods producers produced slightly less than in the previous period.

Production, manufacturing



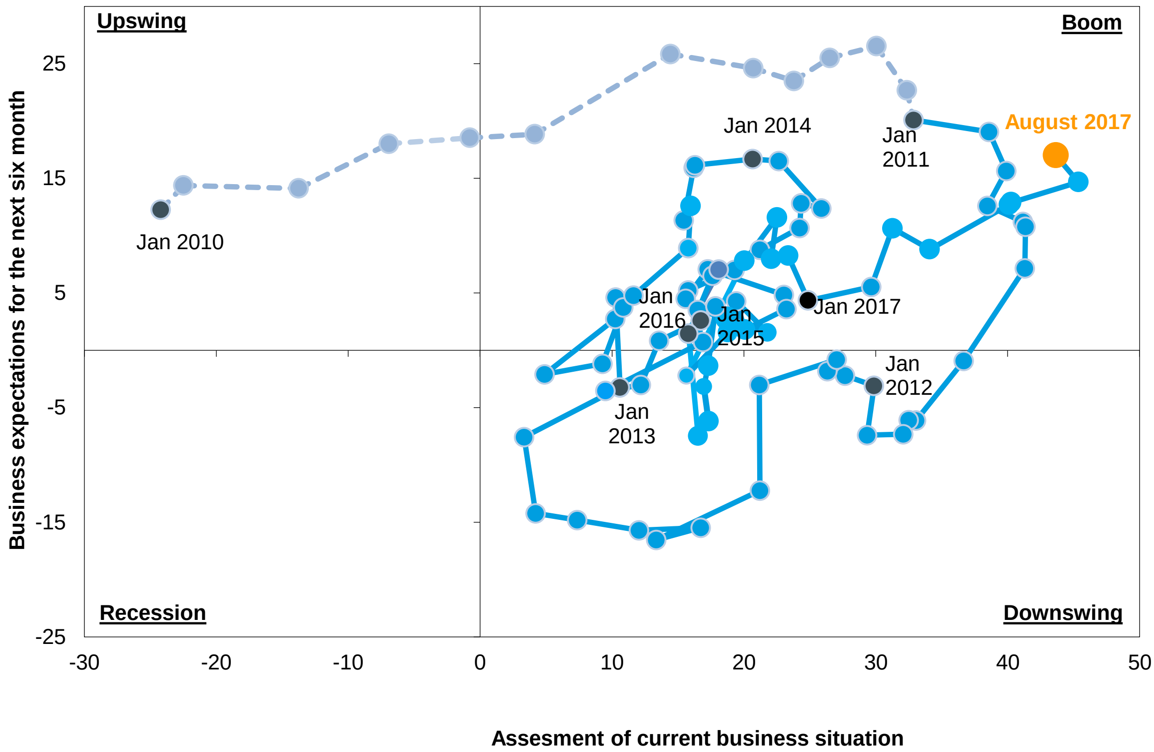
Source: Federal Statistical Office

All in all, the second quarter results were exceptionally good. German industry not only managed to increase its output for the sixth quarter in a row (year on year), but the increase was the biggest quarterly hike seen in more than three years. Production expanded equally across all **main industrial groups**. In view of the high level of incoming orders, full order books and good sentiment indicators, the clear upward trend in production is set to continue for the medium term.

Industrial capacity utilisation rising constantly

Expanding production levels in industry has made capacity utilisation rise even higher. In the second quarter, the industrial capacity utilisation rate reached 86 percent for the first time since 2008. In the third quarter 2017, capacity utilisation in manufacturing even measured 86.7 percent. This puts current capacity utilisation 3.6 percentage points higher than the average rate over the last ten years. The order backlog in industry, at an average of 3.2 production months, is exceptionally high. Over the past 30 years, the order backlog has moved between 2.4 and 3.4 months. At 0.4 production months over the ten-year average, orders are as high as they were in 2007 and 2008.

ifo Business-Cycle Clock
German manufacturing*



* Balances, seasonally adjusted

Source: ifo Institut

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Business climate: business prospects remain high

The sentiment in **German trade and industry** clouded over slightly recently. The ifo business climate index slipped by 0.1 points in August, down to 115.9 points. The minor drop in sentiment was caused by a less optimistic view of the current situation, while the component of future prospects improved for the fourth time in a row. Among the individual sectors, expectations in the trade sector were slightly negative. In **wholesale** the business climate deteriorated due to a lower rating of the current situation. Prospects, in contrast, improved slightly. Sentiment in **retail** was down substantially. The current situation is regarded with much less optimism, and prospects as slightly lower. The automotive retail sector, in particular, pulled down sentiment. The business climate index in the **building industry proper** rose to a new record high. The surveyed companies regarded both the current situation and business prospects as improved. Sentiment in **manufacturing** even managed to top the record value set the previous month. After eight months of trending positively, the current situation is no longer quite as good, but business prospects for the next six months improved substantially. Companies did not assess their export prospects quite as positively as previously, their rating here going down by 1.1 percentage points.

Outlook

Stable growth at start of year

With annualised growth rates of more than two percent in each of the first two quarters of the year, the German economy has expanded at a surprisingly strong pace so far. Private consumption and foreign trade have outperformed our expectations considerably. We therefore need to adjust our growth forecast for the current year.

The main driver of economic growth in Germany in the second half of the year is likely to be **private consumption**, buoyed particularly by the continuing increase in jobs subject to social security contributions. Sentiment among consumers is correspondingly high. The consumer climate, as measured by market research company GfK, reached its highest level since October 2001 this August. Consumers' income prospects have increased constantly in the last five months. The propensity to purchase larger items has also risen substantially, fuelled by the solid employment situation in Germany. We are now expecting private consumption expenditure to increase by 1.8 percent. **Public consumption expenditure**, on the other hand, has not increased as much as expected at the start of the year. In view of the figures for the first half of the year, we now expect an annual increase here of two percent.

BDI forecast for 2017 and comparison: real economic output, change over previous year

	BDI	Federal Government	European Commission
GDP, real	1.8	1.4	1.6
Consumption	1.9	-	-
- Private Consumption	1.8	1.4	1.3
- Public Consumption	2.0	2.3	3.2
Investment	2.9	1.7	1.9
- Construction	3.0	1.9	-
- Machinery and Equipment	2.5	1.2	1.4
- Other	3.2	2.2	-
Exports	4.0	2.8	3.7
Imports	5.0	3.8	4.8
Net Exports, Economic Output	-0.1	-0.1	-0.1

Sources: Federal Government, European Commission (May 2017), own calculations

Investment activity is developing in line with our estimates. Although **investment in plant and equipment** was slightly below our expectations in the first six months of the year, we still believe that growth of 2.5 percent is realistic as industrial capacity utilisation is at such a high level and recent figures show that it has risen still further. For **construction investment** we maintain our forecast of a three percent increase. Construction output and buildings completed even recorded a slightly higher rise in the first half of the year. The prospects for residential construction remain good considering the high demand for residential space and rising building permit figures. In view of the funds provided for federal truck road construction, among other things, public sector construction is also set to increase further. The construction industry also anticipates continued growth in commercial construction. **Investment in other assets** (software, research and development) has recorded such a steep increase in the first half of the year that we now expect a rise for the year overall of 3.5 percent.

Exports recorded much stronger growth in the first half of the year than we expected. Germany's foreign trade benefited in particular from the general economic recovery in Asia (Global Growth Outlook 2017). German exports received further momentum from the broad upturn in Europe. The risks ensuing from Brexit and the new US administration have not materialised in full so that the **exports of goods and services** in the current year should increase by four percent. Rising exports also drive up imports, on account of supply chain structures, which should also expand on the back of stronger consumption expenditure. We now anticipate imports to increase by five percent, which would result in net exports only nudging GDP growth down by 0.1 percentage points.

All in all, the Germany economy is growing at a much faster pace than anticipated at the start of the year. We now expect real economic output to increase for the year overall by **1.8 percent** over the previous year, which corresponds to growth of just over two percent after calendar adjustment.

Sources

BDI (2017). Global Growth Outlook. Berlin. August.

Imprint

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Basic data for national accounts

GDP (price, seasonally and calendar adjusted)
Change over previous period in percent

			2016				2017	
	2015	2016	Q1	Q2	Q3	Q4	Q1	Q2
Consumption	2.2	2.5	0.8	0.3	0.3	0.6	0.3	0.8
-Private Consumption	2.0	2.0	0.6	0.2	0.4	0.6	0.4	0.8
-Public Consumption	2.7	4.0	1.5	0.7	0.2	0.5	0.2	0.6
Investment	1.7	2.3	1.2	-1.2	0.5	0.0	2.7	1.0
-Machinery and Equipment	3.7	1.1	0.4	-1.8	0.7	-1.3	2.1	1.2
-Construction	0.3	3.0	2.0	-1.8	0.2	1.0	3.4	0.9
-Other	1.9	2.6	1.0	1.3	0.9	-0.4	2.0	0.9
Domestic Demand	1.6	2.3	0.9	-0.2	0.8	0.8	0.1	1.0
Exports	5.2	2.6	1.0	1.3	-0.2	1.3	1.6	0.7
Imports	5.5	3.7	1.7	-0.2	0.7	2.5	0.4	1.7
Total	1.7	1.9	0.6	0.5	0.3	0.4	0.7	0.6

Contribution to growth (in percentage points)

Consumption	1.6	1.8	0.6	0.2	0.2	0.4	0.2	0.6
-Private Consumption	1.1	1.1	0.3	0.1	0.2	0.3	0.2	0.4
-Public Consumption	0.5	0.8	0.3	0.1	0.0	0.1	0.0	0.1
Investment	0.3	0.5	0.3	-0.2	0.1	0.0	0.6	0.2
- Machinery and Equipment	0.2	0.1	0.0	-0.1	0.1	-0.1	0.1	0.1
-Construction	0.0	0.3	0.2	-0.2	0.0	0.1	0.3	0.1
-Other	0.1	0.1	0.0	0.1	0.0	0.0	0.1	0.0
Change in stocks and the like	0.0	-0.2	0.0	-0.2	0.4	0.3	-0.7	0.2
Domestic Demand	1.5	2.1	0.8	-0.2	0.7	0.8	0.1	1.0
Net Exports	0.2	-0.2	-0.2	0.7	-0.4	-0.4	0.6	-0.3

Source: Destatis