

7 August 2008

# Economic News

## GROWTH IN GERMANY

### The boom years of industrial growth are over for now

- Germany is experiencing an industrial downturn, as is increasingly evident following the publication of recent order and production data. The rapidly shrinking order backlog is pulling production down with it. The strong euro, the economic slowdown among the most important trading partners, rising input costs and the winding down of the global investment boom are increasingly taking their toll.
- German industry boomed for nearly five years, largely attributable to sweeping restructuring and modernisation measures that led to a significant improvement in competitiveness. For a long time the appreciation of the euro was absorbed virtually effortlessly, as unit labour costs declined markedly due to moderate wage increases and accelerated productivity gains.
- As difficult as it is to believe, the boom years are over for now and the German industry is currently in a downturn. Since November 2007, new factory orders have fallen for seven consecutive months, declining by a total of nearly 9%, with non-domestic new orders down by over 12% and domestic new orders down by nearly 5%.
- There are many reasons for the downturn, ranging from the slowdown in global economic growth to the appreciation of the euro, the sharp increase in input costs and the winding down of the investment boom in Germany and many other countries. With regard to Germany's non-domestic industrial activities, many of its major trading partners in the EU, which is its most important non-domestic market, are currently on the verge of a recession. We will also have to get accustomed to the idea that, in view of the substantial wage increases, unit labour costs will not drop in the future, particularly since productivity growth is slowing for cyclical reasons.
- Accordingly, the slowdown in industrial production going forward is likely to further dampen overall economic growth. Although Germany's industrial output in June increased slightly (+0.5% m/m), it was 1.6% lower overall in the second quarter compared to the first. Although many companies continue to have well-filled order books, production growth looks set to ease as increasingly fewer new orders are being placed. Hence, with capacity utilisation expected to gradually decline, the labour market is unlikely to receive a boost in the second half-year. On the contrary, cost savings strategies are expected in many areas, with the result that employment in the industrial sector will decline by the end of the year.

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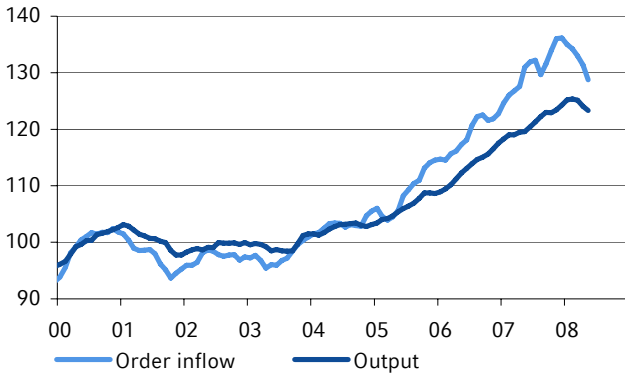
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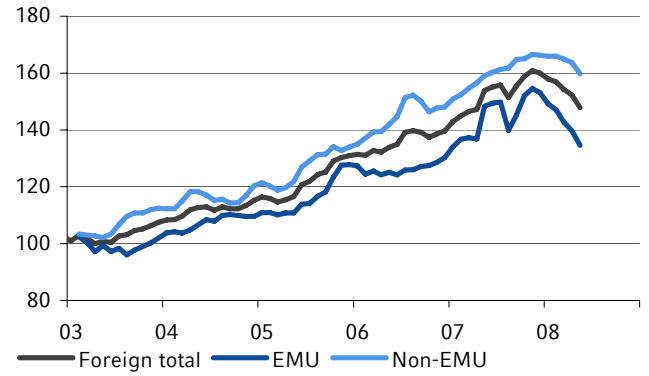
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**Manufacturing orders and output**  
2000 = 100



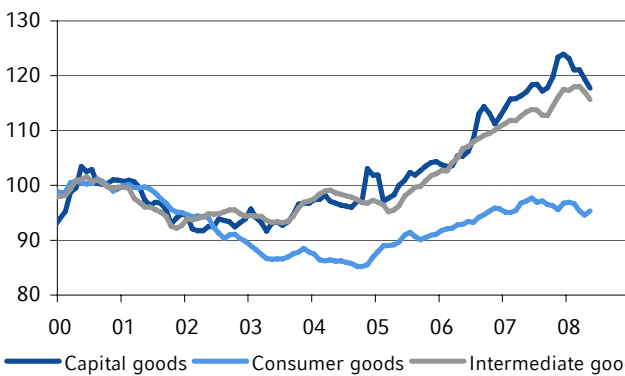
Source EcoWin, WestLB Research

**Foreign manufacturing orders inflow**  
2000 = 100



Source EcoWin, WestLB Research

**Domestic manufacturing orders**  
2000 = 100



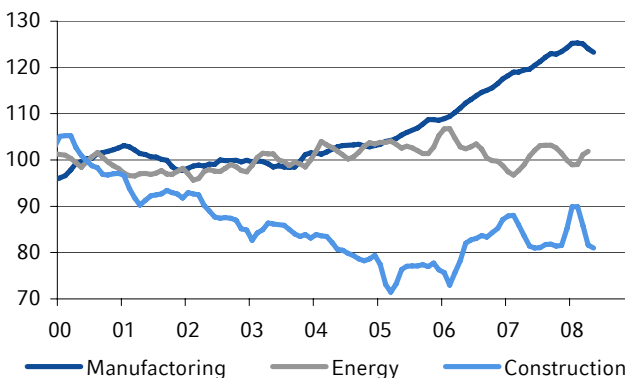
Source EcoWin, WestLB Research

**Foreign manufacturing orders inflow**  
2000 = 100



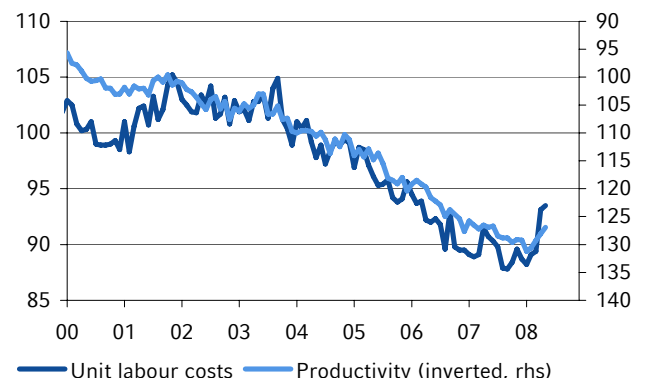
Source EcoWin, WestLB Research

**Industry production**  
2000 = 100



Source EcoWin, WestLB Research

**Unit labour costs and productivity**  
2000 = 100



Source EcoWin, WestLB Research

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