



Economic Forecast Germany 2015/16

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Berlin (gtai) - Higher employment levels and real wages lead to an increase in private consumption expenditures. Households thus contribute the most to further growth of the German Gross Domestic Product (GDP). Demand is additionally stimulated by public sector activities. On the other hand, weakening impulses emanating from foreign purchases should lastly channel economic endeavors into a moderate upward trend. In this light a more pronounced expansion of productive capacities may not be a viable course of development, members of the German Council of Economic Experts (GCEE) say.

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1 General Economic Outlook

Development of Gross Domestic Product

Germany is trending towards a somewhat unspectacular increase in business activities. This assessment may be found in the fall 2015 version of the Joint Economic Forecast published by several leading research institutions. Furthermore, GDP is growing at similar rates as potential output, and the estimated difference between these two measures has been converging to zero for some time. Therefore, many companies have already reached the limits of their production capacities. Despite such constraints and mostly transitory stimulating effects caused by low interest rates and fuel prices, by an improved competitiveness on markets outside the European Community (EU) due to a devalued Euro, and consequently by an increased purchasing power for consumers experts rule out a more pronounced expansion. The sluggish pace of the economy in several world regions is one of the reasons given.

Change of Principal Macroeconomic Aggregates 2014 to 2016 (in %, on a price-adjusted basis)

	2014	2015 *)	2016*)
GDP	1.6	1.8	1.8
Exports of goods	4.2	6.3	5.0
Gross fixed capital formation	3.5	2.4	2.7
Private final consumption	0.9	1.9	1.8

*) Forecast

Sources: Joint Economic Forecast of the German Institute for Economic Research (DIW Berlin), of the Ifo Institute (Munich), of the Halle Institute for Economic Research (IWH), and of the Rheinisch-Westfälisches Institut für Wirtschaftsforschung (RWI Essen); Federal Statistical Office

With a view towards the risks inherent in forecasts the research institutes consider that realistically GDP growth in 2015 may end up in an interval of 1.6 to 2.0% (confidence level of 68%). For 2016 the margin is widened to 0.3 and 3.3%. Data presented by the Federal Statistics Office show modest GDP growth rates for the first three quarters of 2015; the figures imply an average of 0.33% compared to the respective preceding three months (corrected for seasonal and calendar influences). Uncertainties on the road ahead possibly include shocks related to a surging stream of foreign migrants.

Fiscal policy is said to be expansive. For the period ranging from 2016 to 2018 Federal government put an investment package worth 10 bn Euros in place. Selected local administrations exhibiting insufficient financial resources will receive funds from a newly created investment facility. The German economy is stimulated additionally by tax relief



measures: In January 2016 personal and child exemptions are raised and the "hidden tax increases" ascribed to the combination of higher incomes and progressive rates are reduced. Retired workers will benefit from higher pensions. Lastly, the scope of reimbursements by the mandatory nursery care insurance is broadened and numerous foreign migrants may be eligible for receiving transfer payments by general government. The fiscal impact totals almost 9 bn Euro in 2016 or 0.3% of GDP.

In a longer term perspective, however, the need to focus on the future viability of the German economy should be addressed, the GCEE asserts. One of the questions to be answered involves the issue of how to reverse the slowdown of productivity growth. At present there are only few signs pointing to a reversal of past and current trends. Solutions may be found in a successful digital transformation of the entire economy since on the aggregate German businesses have not yet managed to augment productivity as effectively as for instance their counterparts in the USA through the employment of information and communication technologies (ICT).

Key Economic Indicators

Indicator	2014	2015 1)	2016 1)
GDP (current prices, bn Euro)	2,915.7	3,025.6	3,121.7
GDP per capita (Euro)	36,041	37,261	38,350
Population (mn) 2)	80.9	81.2	81.4

1) Forecast; 2) Midyear estimates on the basis of the 13th coordinated population projection for Germany (2015), scenario "continuity with moderate immigration"; because exact data for recent migratory movements are not available the figures do not reflect events having taken place in the recent past

Sources: Joint Economic Forecast of DIW, IFO, IWH-Halle und RWI Essen; Federal Statistical Office

Gross Capital Formation

The European Central Bank is maintaining its monetary policy until further notice. It is to be expected that interest rates remain extremely low compared to historic levels. According to surveys conducted by the IFO Institute few companies complain about restrictive lending practices in the banking sector (September 2015: 14.8%). Slightly more problems were encountered by small manufacturing establishments and by the construction industry during the same month (17.7% each).

Bank loans to the private sector increased by 1.9% to 2.41 bn Euros in the period starting June 2014 and ending June 2015 (previous twelve months: -0.4% to 2.37 bn), the German Central Bank (Bundesbank) reported. Loans for residential construction rose by 3.1% to 1.21 bn Euros.

Purchases of machinery and equipment are projected to grow by 4.4% in 2015 and by 3.7% in 2016 according to the Joint Forecast of major economic research institutes. For both years the sales outlook appears increasingly favorable. On the other hand, macroeconomic capacity utilization will not surpass values that usually are considered as "normal" by much. Generally expansion investment will be playing only a minor role. As to construction, experts believe that growth rates of 1.0% in 2015 and of 2.1% in 2016 (2014: 2.9%) are in order.

Surprisingly, most of the economic research institutes are convinced that business managers continue to lower inventories up to 2017. Data published by the Federal Statistics Office show that the trend began in 2012 (reduction of 12.3 bn Euros; 2013: -10.5 bn; 2014: -22.0 bn Euros).

Private Consumption Expenditures

The Macroeconomic Policy Institute calculates that private consumption expenditures contribute more than half to GDP growth in 2015 and 2016. Households remain the most important driver for the near term economic development in Germany. Private purchases are fuelled by substantial increases in gross earnings (3.9% in 2015 as well as in 2016). Furthermore, the number of employed workers rises from 42.8 mn to 43.0 mn persons (2014: 42.6 mn). Concurrently the unemployment rate as defined by the Federal Employment Agency decreases from 6.4 to 6.3% (2014: 6.7%). The purchasing power of wages is strengthened additionally by a variation of consumer prices that in the eyes of several research organizations should amount to only +1.1% in 2016, (2015: +0.3%; 2014: +0,9%).

Business representatives characterize the retail environment as "good". Real wages are rising, occupation is high and inflation low, observe members of the German Retail Association. Aggregate revenues will amount to 469 bn Euros in 2015 (+2% compared to 2014) with multi-channel retailers being especially optimistic. Online activities will bring in 41.7 bn Euros (+12%). During 2015 stores selling cosmetics and personal care items, watches and jewelry, consumer electronics and furniture reported above average results.

Foreign Trade

German exports will increase by 6.8% in 2016 and by 6.4% in 2017, publications of the Kiel Institute for the World Economy (IfW) reveal. Shipments to other countries are supported by the economic recovery in the Euro zone and by robust growth rates in the



USA. In a medium term outlook German global price competitiveness should not deteriorate. Germany benefitted from changes in relative international prices due to the devaluation of the Euro against major currencies.

Because of the flourishing export sector and expected increments in private consumption and investments imports will grow by 8.1% in 2016 and by 7.6% in 2017, IfW researchers argue. It cannot be ruled out that Germany's Terms of Trade will improve again. In such a scenario modestly lower import prices will combine with slightly inflationary export prices.

German Foreign Trade (in mn Euro; variation compared to previous year's results in %)

	2013	2014	2015 1st half	Variation 2015/2014
Imports	898.2	916.6	471.3	2.9
Exports	1,093.1	1,133.5	595.1	6.9
Balance of Trade	195.0	216.9	123.8	25.4

Quelle: Federal Statistical Office

Germany's current account surplus most likely rises by one percentage point to reach 8.5% of GDP in 2015 according to the already mentioned Joint Forecast. About three fourths of the increase may be attributed to price reductions on the global markets for oil and petroleum products. In 2016 the balance in the current account should amount to 8.3% of GDP.

Exports by SITC based commodity groups (in mn Euro; variation compared to previous year's results in %)

SITC Commodity Group	2013	2014	2015 1st half	Variation 2015/2014
0 Food and live animals	51.5	52.5	25.8	0.1
5 Chemicals and related products	172.7	178.6	94.4	5.7
.51 Organic chemicals	24.3	24.4	12.2	-1.4
.54 Medicinal and pharmaceutical products	57.0	60.4	33.3	13.4
.57 Plastics in primary forms	23.6	24.2	12.5	0.5
6 Manufactured goods classified chiefly by material	139.2	141.1	72.4	1.7
.67 Iron and steel	24.9	24.1	12.6	2.9
7 Machinery and transport equipment	523.7	545.5	290.7	9.3
.71 Power generating machinery and equipment	41.0	42.4	22.2	5.0
.72 Machinery specialized for particular industries	46.8	46.3	23.2	1.2
.74 General industrial machinery and equipment	79.4	82.4	41.9	4.2



.77 Electrical machinery, apparatus and appliances	80.9	83.7	44.0	7.5
.78 Road vehicles	182.1	194.2	107.8	11.4
8 Miscellaneous manufactured articles	111.4	115.7	59.1	6.0
.87 Professional, scientific and controlling instruments and apparatus	37.0	38.3	20.0	7.0

Source: Federal Statistical Office

2 Trends in Selected Industries

Although exceptional business conditions that include a "weak Euro", "inexpensive oil" and "low interest rates" generally favor economic expansion output in the manufacturing sector increases only by a low margin, remark analysts at the German Chemical Industry Association (VCI). In some industries businesses hesitated to build up inventories. Developments in the global demand for investment goods led to diminished production activities in several German markets.

Nevertheless, the utilization of productive capacity in manufacturing companies has frequently exceeded levels that experts generally describe as "normal". Starting in the 4th quarter of 2013 the values of the order-capacity-index calculated by the Bundesbank illustrate that establishments receive more orders than they actually are able to fulfill with existing production facilities.

Mechanical Engineering

Economists at the German Engineering Federation or VDMA reckon that member companies will be confronted with stagnating sales in 2015 as well as in 2016 (2014: +1.1% to 199 bn Euros). Mechanical engineers have had to adjust to a worsening investment climate influenced by political turbulences, by suboptimal market developments such as in China or by the continuing debate about the future of the European currency, commented VDMA president Reinhold Festge. On a positive note reindustrialization in the USA is staying its course, and the investment shortfall in the European Union seems to be vanishing. Builders of machinery and equipment utilized their capacities to 84.8% in July 2015 which was only minimally below the long term average.

Automotive Industry



Companies manufacturing motor vehicles will most likely invest 16 bn to 18 bn Euros until 2020 to enable networked and automated driving. Towards the end of 2017 an internet connection should be installed in a projected 80% of newly produced cars, envisioned Mathias Wissmann, president of the German Association of the Automotive Industry (VDA) on the occasion of the 66. International Motor Show. In the first nine months of 2015 registration of new automobiles increased by 5.5% to 2.41 mn units and of trucks by 1.6% to 0.19 mn. Production of light vehicles displayed a plus of 2.1% to 4.33 mn units, exports a hike of 2.7% to 3.35 mn. The complete year may end with an output increment of 2.0%, forecasts the VDA. In 2014 about 5.6 mn units left the assembly lines. According to the Center for Automobile Management in 2015 registrations should be 4.5% above the 2014 level (3.2 mn units).

Chemical Industries

The sector will probably report the following results for 2015, VCI sources say: an output increase of 1.5%, stagnating sales of approximately 191 bn Euros, and lower average sales prices of 2.5%. While revenues may decrease in the domestic market turnover will rise moderately beyond German borders. Obviously, companies are also able to conduct business under difficult global economic conditions, explain spokespersons for the association. Yet, chemical enterprises do not consider any improvements of their situation to occur in the short run. Therefore the roller coaster ride of the industry will continue for a while. Growth prospects remain modest. Positive signals are spotted in other EU member countries.

Construction Industries

In view of well-filled order books the outlook for construction investment is promising. Analysts at IWF Kiel conclude that the value of residential construction will expand by 3.0% in 2015. During 2016 and 2017 growth accelerates to 3.5 and 3.8% respectively. Public sector activities intensify because of support programs for local governments and due to investment initiatives pursued on the federal level. Construction by general government increases by 3.0% in 2016 and by 3.5% in 2017 escaping from the stagnation observed in 2015. The start of building projects in the business world is going to be stimulated by a favorable investment climate and capacity shortages (2015: -2.0%; 2016: +1.3%; 2017: +2.4%).

Electronic and Electrical Engineering

About two thirds of German electrical and electronic engineering companies expected that business climate would not change significantly in the six months following

September 2015. Only 19% considered an improvement. According to the German Electrical and Electronic Manufacturers' Association or ZVEI incoming orders grew by 6.3% during the first nine months compared to the same period in 2014. Orders from other countries ended up with a plus of 10.4%. However, output increased only by 0.6% in inflation adjusted terms from January to September 2015. Sales, on the other hand, amounted to 130.7 bn Euros and were 3.7% higher than in the previous year. Minor revenues of 0.8% in the domestic market (62.9 bn Euros) were compensated by a surge of 7.9% beyond national borders (67.8 bn Euros).

Information and Communication Technologies

Information technology companies (IT) continue to sit in the driver's seat of the ICT sector. IT-sales should increase by 3.5% to 80.4 bn Euros in 2015 according to the trade association Bitcom. Within the IT-area software revenues grow the most: 5.4% to 20.1 bn Euros. Turnover in the IT-services business including consulting and project development has been reaching constantly new heights; sales are forecast to finish 2015 with 37.3 bn Euros implying a plus of 3.0% compared to 2014. Bitcom described recent developments in the IT-hardware segment as "surprisingly positive" (2015: +2.8% to 23.0 bn Euros). Satisfying the demand for telephone devices and for infrastructure systems will contribute to a growth of 0.9% in the telecommunications business; this will mean revenues of 65.8 bn Euros in 2015. Total sales of the ICT sector should exhibit a plus of 1.5%.

Environmental Technologies

The German economic environment of 2015 is conducive to improve business in the heating equipment market. A projected plus of around 5% to 0.71 mn units is in the cards, spokespersons for the Federal Association of German Heating Industry or BDH say. Lower fuel prices favor purchases of oil based equipment. Demand is also stimulated by the age of the existing stock: More than 70% of heating devices in use do not incorporate state of the art technologies. Leaders engaged in water management will need to concentrate on reducing nutrients, pesticides and pharmaceutical waste, maintains the German Association of Energy and Water Industries or BDEW. A 91% of manufacturers in the waste and recycling segment envisioned that their revenues increase or remain the same in 2015. A proposed law governing the use of recoverable residual materials should lead to increased recycling rates.

Medical Devices

Demographic changes and the introduction of new methods for therapy help increase sale volumes which should lead to higher revenues of 4.3% in the German market for medical devices, claims the German Medical Technology Association (BVMed). Export markets will show a plus of 6.8% in 2015. Looking to 2016, only 43% of surveyed companies expected better business conditions within national borders, but 62% did so with a view of the rest of the world. In 2014 revenues in the domestic market grew by 2.9% to 8.1 bn Euros while income derived from sales abroad grossed 17.1 bn (+2.0%). BVMed considers cardiology, oncology, neurology, diagnostics, orthopaedics and surgery to be the most innovative areas for research and development. Lastly, proposed new EU regulations will significantly impact German companies in the future.

Logistics

Total transport volume is increasing by an average annual growth rate of 0.4% and will reach 4.2 bn metric tons per year in 2017 according to the Federal Ministry of Transport and Digital Infrastructure. During the same period the performance of the sector is expanding by some 1% per year to 674.8 bn ton-kilometers (metric). Border crossing traffic will intensify much stronger than domestic freight movements. Surveys conducted by the German Logistics Association (BVL) in the third quarter of 2015 among service providers, retailers, wholesalers and manufacturing companies indicated a slightly less optimistic mood than in previous periods. However, BVL leaders were still convinced that the year of 2015 was going to end with a new record as far as revenues are concerned (2014: 235 bn Euros).

Wind power

German federal legislators plan to modify current regulations for the renewable energy sector in 2016. This may imply that promotion of eolic energy projects will be based on still to be defined public tender mechanisms from 2017 on. The German Wind Energy Association (BWE) estimated that in 2015 new onshore generating capacities will show a net increase in the order of 4.000 to 4.500 MW (2014: 4.386 MW). During the first six months only 1.093 MW were installed; that was 34% less than the equivalent value for 2014. Furthermore, a total of 422 offshore plants with an aggregate capacity of 1.765 MW were added to the power grid in the first half of 2015. As to the entire year new generation equipment outside Germany's coast line will provide for 2.250 MW.

Food Processing and Marketing

A stronger diversification of the demand for food products seemed to be one of the trends observed during the 2015 version of the Anuga trade show. Traditional habits

are giving way to more complex preference patterns. Generally, however, a stagnating domestic market, an oscillating export business, high production costs and an intensive global competition exert pressure on operating margins and jobs, analysts at the Federation of German Food and Drink Industries (BVE) explain. During the first half of 2015 food sales diminished by 4.4% to 81.9 bn Euros when compared to January-June 2014. Within national boundaries the revenue slump was even more pronounced: - 6.5% to 55.8 bn Euros. The disappointing results for the industry are mainly the consequence of lower prices at home and abroad.

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