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# GERMAN OUTPUT: JUNE PARTLY OFFSETS MAY SURGE

## Berenberg Macro Flash

**German industrial production (incl. construction), June, in %**

| | mom | yoy |
|---|---|---|
| **Actual:** | **-0.9** | **2.5** |
| Previous: | 2.4 | 3.0 |
| Consensus: | -0.5 | 3.0 |
| Berenberg: | -0.3 | 3.3 |

**Despite a setback in June, German industry continues to grow on trend:** A modest gain in industrial output in Q2 after stagnation in Q1 suggests that German GDP probably expanded at a less subdued rate in Q2 than the 0.3% qoq registered in Q1. After today's reading, we maintain our call that German GDP growth probably increased by 0.5% qoq in Q2 driven by the partial bounce-back of industrial production and a recovery in retail and services.

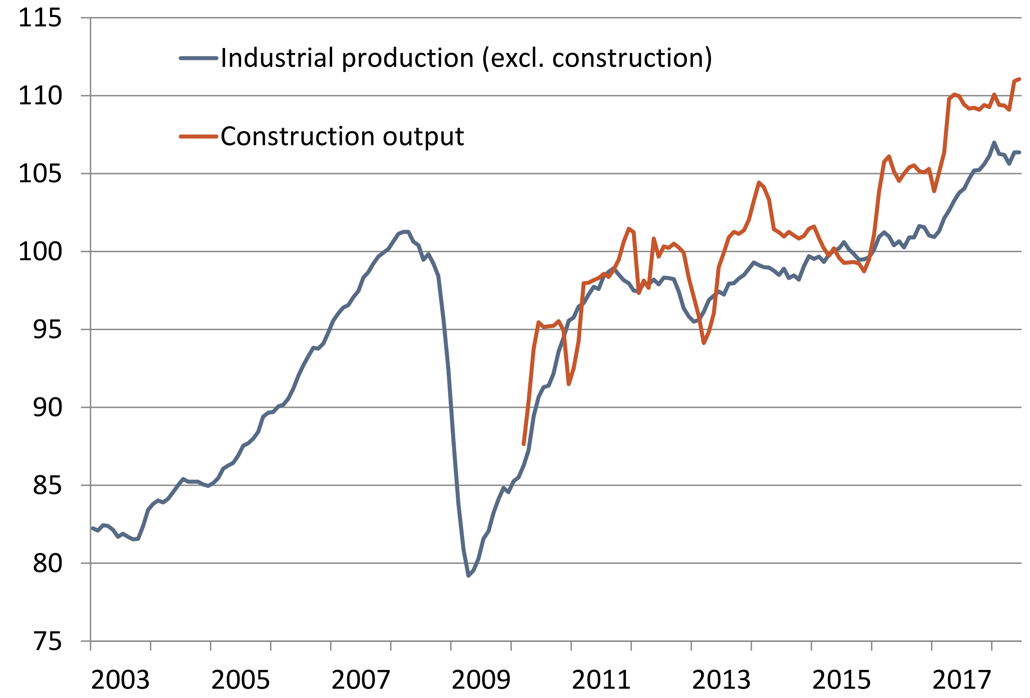
**In June, German industrial production cooled by more than expected:** After the 2.4% mom surge in May, output dropped by 0.9%. The losses were broad-based: manufacturing (and mining), making up for 80% of total output, fell by 0.9% mom (intermediate goods: -0.8%; capital goods: -0.6%; consumer goods: -1.6%). Construction (14%) suffered a bigger hit of 3.2%. Output excluding construction, which is comparable with the industrial production data reported by Eurostat, dropped by 0.6% mom. Energy production gained 2.9% mom, but given its small share of total production (6%), it could not offset the losses of the other two sectors.

**Industrial production is a bellwether for the overall economy, but monthly data can be volatile**, so we should take the usual ups and downs with a pinch of salt. On an annual basis, industrial production including construction has gained 2.5% vs. June 2017, after 3.0% in June (see chart 1). Comparing Q2 with Q1, output expanded by 0.4% qoq after stagnating in the previous quarter. It could contribute up to 0.1ppt to German GDP growth. The first estimate for GDP will be published on 14 August.

**The times of the exceptionally strong gains of 2017 during which output expanded by 1.2% qoq on average are clearly over.** Yesterday's disappointing factory orders (-4% mom in June), which lead output by roughly 2 months on an annual basis (R-squared: 87%), and unchanged export data for June (vs. May, also released today) add to the impression that the trade tensions continue to cast dark shadows over the German economy. Yet, June and July were the time during which US-EU trade tensions peaked. While uncertainty about the future trading regime persists, the US-EU agreement brokered on 25 July to negotiate instead of slugging it out in tit-for-tat retaliation has reduced the risk of a genuine transatlantic trade war for the time being. Some stabilisation in survey data released for July, and even a rebound in new manufacturing orders according to the PMI survey (see chart 2), suggest the worst may be over and we could slowly return to a calmer environment in H2.

**Going forward, supply bottlenecks may restrict the pace by which German production can expand as much as the uncertainty arising from the trade tensions.** The unemployment rate is at a multi-decade low of 3.4% and capacity utilisation has risen to 88%, the highest level since early 2008. While this constrains the expansion of output, it should also continue to keep the pressure on German manufacturers to invest in their production capacities elevated which would bode well for the outlook for late 2018. From Q4 onwards we expect the German economy to expand by 0.5% qoq and 2% yoy.

**Chart 1: German industrial and construction output since 2003**




*Indexed at 2015=100. Source: Destatis*

Chart 2: German factory orders (yoy, in %) versus PMI new manufacturing orders


*Sources: Destatis, Markit*



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