

## German industry stagnates at too low level

Industrial activity in November provided more evidence that the economy did not fall off a cliff in the fourth quarter but was not strong enough to avoid a contraction either



German industrial production increased by 0.2% month-on-month in November, from a downwardly revised -0.4% MoM in October. On the year, industrial production was down by 0.4%. Production in the energy-intensive sectors increased by 0.2% MoM and is now down by almost 13% compared with November last year. While production in the energy sector increased by 3% MoM, activity in the construction sector weakened by 2.2% MoM.

### Glass half full or half empty?

Today's industrial production data brings back the old question of whether the glass is half full or half empty. To some, the current stagnation means that German industry is holding up better than feared. To others, it is only filled order books at the start of the war in Ukraine and the backlog of orders that prevented more severe damage to industrial production. In any case, industrial production is still some 4% below its pre-pandemic level. Almost three years after the start of the pandemic.

The former growth engine of the German economy is stuttering and improvement is not really in sight. Despite the recent return of optimism as illustrated by improving sentiment indicators, the

sharp drop in new orders, the inventory build-up in recent months, the lagged impact of high energy prices and potential supply chain frictions as a result of China's Covid policies all bode ill for the short-term outlook.

Still, the New Year started on a more optimistic footing for the German economy. The mild temperatures almost seem to have ended the energy supply crisis, at least for now. National gas reserves have increased again, and consumption is clearly below historical averages. However, the question is how sustainable the safety net of warmer temperatures and fiscal stimulus can be. Even at the risk of being perceived as the boy who cried wolf, the short period in early December when a real winter spell pushed gas consumption more than 10% above historical averages illustrates how deceptive the optimism at the start of the year could be. Let's not forget that the German economy is still facing a series of challenges which are likely to weigh on growth this year: energy supply in the winter of 2023/24, changing global trade with more geopolitical risks and changes to supply chains, high investment needs for digitalisation and infrastructure and an increasing lack of skilled workers. While the warm weather should actually ring alarm bells in terms of climate change, it is a welcome surprise for the economy. However, the warm weather does not simply blow away all economic problems.

## Solid construction sector too little to avoid recession

Today's industrial production data was the last hard macro data before the German statistical office releases its first estimate of fourth-quarter growth. Remember that in the third quarter, soft data plunged like a stone although actual GDP growth surprised to the upside. This time around, it looks as if hard data will be catching up. So far, and compared with the third quarter, retail sales, exports and industrial production all point to a mild contraction in the economy. Only the construction sector seems to be in growth territory. Despite the latest improvements in confidence indicators, available hard data still suggests that the economy's slide into recession has continued.

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