

## Latest industrial data shows what the German economy could have looked like

Industrial production grew in February, adding to the positive macro data in the first two months of the year. It will be the last positive macro news for a while. The war in Ukraine has drastically changed the German growth outlook



Despite improvements in monthly data, we believe it's still too early to call a rebound in Italian industrial production

Industrial production increased by 0.2% month-on-month in February, from 1.4% in January, sending the last signal of what the German economy could have looked like had the war in Ukraine not happened. Over the year, industrial production was up 3.2%. Still, industrial production is almost 4% below its pre-pandemic level.

### Impact of the war in Ukraine not yet visible in hard data

With today's industrial production data, we have the full batch of the first two months of the year for the German economy. The picture these data paint is still one of an economy that is about to pick up speed. Retail sales stagnated but didn't fall under high energy prices; net exports increased and industrial production was clearly up compared with the fourth quarter of 2021. Based on these developments in the first two months of the year, the German economy was on track for slightly positive growth in the first quarter and a significant rebound thereafter. Well, all of this was before

the war.

The war in Ukraine has not only dramatically changed the world but also the outlook for the German economy. Higher energy and commodity prices than at the start of the year and probably for a long time, new supply chain disruptions on top of the old ones with a high risk that these will be disrupted for good, and elevated uncertainty and fear will weigh on both supply and demand in the coming months. Real disposable incomes of households will suffer, and companies will have increasing difficulties dealing with the costs of higher energy and commodity prices, putting corporate profit margins under pressure. The first soft indicators indeed point to a sharp drop in production expectations and a surge in uncertainty.

## Entire economic model is at risk

Even worse, with high energy and commodity prices for a protracted period, possibly even energy supply interruptions, an acceleration of deglobalisation, and a possible new cold war, an export-oriented economy highly dependent on energy, then of course imports will suffer. Government support schemes will dampen the adverse impact of the war but will not be able to avoid stagflation.

## Recession risk remains

Even with a sharp plunge in economic activity in March, a contraction in the first quarter is not yet a done deal. Looking beyond the first quarter, however, does not paint a rosy picture for the German economy. For the entire year, we recently revised downward our growth forecast to 1.4%, which would delay the return of the economy to pre-pandemic levels until the end of this year.

## Author

### Carsten Brzeski

Global Head of Macro

[carsten.brzeski@ing.de](mailto:carsten.brzeski@ing.de)

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