

■ Economic conditions in Germany

■ Macroeconomic situation

Upturn started to falter in 2011 Q4

The upturn in the German economy started to falter in the fourth quarter of 2011. According to the Federal Statistical Office's flash estimate, real gross domestic product (GDP) in the final three months of the year was 0.2% down on the quarter after seasonal and calendar adjustment. The economic dip, which had been emerging for some months, was triggered by the slowdown in global economic growth combined with perceptible strains on the real economy due to the sovereign debt crisis in the euro area and the uncertainty which this is causing. The decline over the period under review is nevertheless placed into context by the fact that output in some branches of industry achieved a notably high level during the summer months owing to special measures such as shorter or no plant shutdowns. Overall capacity utilisation was at a normal level during the reporting period and calendar-adjusted GDP was 2.0% up on the year.

No change in underlying cyclical trend

Many enterprises have registered this fall in demand, especially for exports, and have clearly made adjustments to their short-term plans. For instance, purchases of intermediate goods have been scaled back and non-urgent investments have been deferred in some cases. By contrast, enterprises are unlikely to have scrutinised their medium to long-term strategic decisions so far, as the disruptive factors are widely regarded as temporary. Personnel planning continued to be shaped by the fact that the search for skilled staff might, if anything, become more difficult. The confidence of households, which was largely unaffected by the uncertainties of the financial markets, was supported by the positive underlying trend in the labour market along with the ample increase in wages. Not only do income expectations clearly contrast with the rather mixed outlook for the economy, there is also – irrespective of the

greater scope for spending – a marked desire to buy, which is tending to buoy consumption.

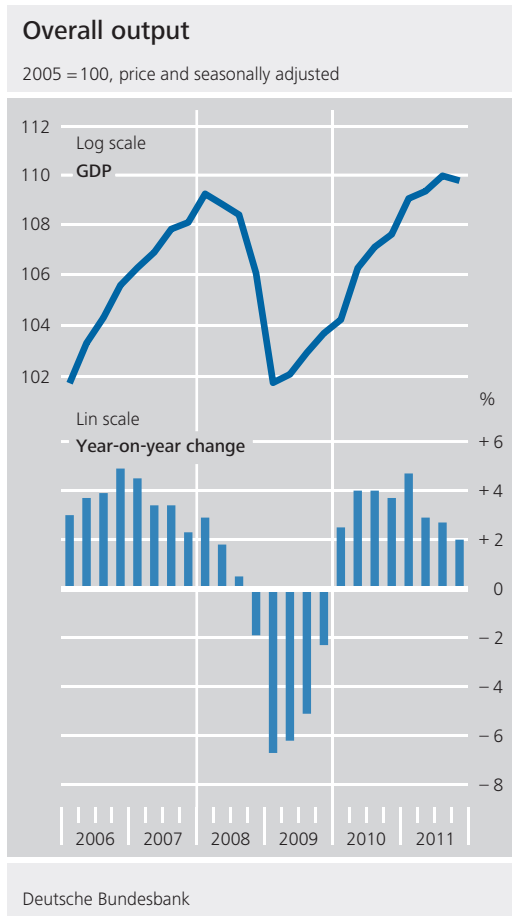
According to the statements of the Federal Statistical Office, private consumption in the fourth quarter of 2011 is unlikely to have maintained its heightened level of the third quarter in seasonally adjusted terms. Despite this, retailers felt an increased eagerness to spend on the part of households in Christmas trading. According to the Ifo business survey, they rated their business situation in December as much better than in the preceding months and also the following January. This conflicts with the official report of nominal retail sales in December: according to current data, this shows a seasonally adjusted fall of ½% compared with November.¹ The quarterly result is thus no more than ¼% higher than retail takings between July and September.

Marked propensity to consume on the part of households

The positive sentiment among households is also a key provider of stimulus for housing construction. Wage growth and the perceived low risk of redundancy, together with financing conditions that continue to be very favourable, have led to more and more households being confident enough to buy their own home. The improved income prospects are also giving impetus to the buy-to-let market, from which investors are evidently primarily expecting the stability of real property ownership at present. Given sharply rising house prices, there is a need for a substantial expansion of the housing stock in order to satisfy the major private and commercial demand for residential property.

Strong impulses from housing construction ...

¹ The current index level for December 2011 in the raw data is 1% higher than the figure first published, which – in contrast to the revised data – received a great deal of public attention. Near-time economic analysis, especially with regard to the assessment of private consumption, is made more difficult by the fact that, since the introduction of the new automatic sample rotation in July 2010, retail sales have been revised upwards by an average of ¾% following the initial publication – a revision pattern that cannot be classified as purely coincidental even taking into account the short observation period.



banks could considerably tighten their credit standards in the near future. Despite certain adjustments of the standards, there is no cause for heightened concern in this regard, however.

The cyclical upturn in investment in machinery and equipment is likely to have been interrupted towards the end of 2011. One reason was that industrial enterprises wanted to wait until they had a clearer idea about the prospects for business before enlarging their machine park. In this connection, it was an advantage that, given the slowdown in demand, capacity utilisation was cut back in the fourth quarter from its very high level during the summer months, which meant that there was less pressure to set up new production facilities. In addition, investment in vehicle fleets had been increasing so strongly well into the third quarter of last year that a lull in the final quarter of 2011 would not be unusual.

Interruption of pick-up in investment in machinery and equipment

Construction firms probably maintained their housing construction activities during the reporting period at least at the same high level in seasonally adjusted terms as in the first nine months of last year, especially as there were no significant weather-related disruptions up to December.

... and from commercial construction

While public sector construction is likely to have suffered a further downturn, heavy use has been made recently of construction sector capacity for commercial buildings, too. In 2011, many enterprises gave priority to the renovation and expansion of business premises over investment in movable fixed assets, the procurement of which had been given preferential tax treatment in 2010 owing to more generous tax depreciation rules. Added to this is the fact that loan financing – which is often used in construction projects on account of the large amounts of investment involved – is decidedly favourable for enterprises, too, at the moment. There may possibly exist some fears that the

The slowdown in global economic activity clearly left its mark on German enterprises' export performance in the fourth quarter of 2011. During the reporting period, there was a seasonally adjusted fall in exports of goods for the first time since the recovery began in mid-2009. Dampening effects came, in particular, from the euro area. The value of goods exports to euro-area partner countries on an average of October and November – more recent data for the regional and goods structure are unavailable at present – was a seasonally adjusted 2¾% down on the average of the preceding quarter. Besides this, sales to neighbouring central and east European countries, including Russia, were also tending to be weak, however. By contrast, exports to China returned to their upward trend following an interruption in growth in the second and third quarters of the year. Moreover, German exporters' business with the United States noticeably picked up momentum. Weaker export demand concerned mainly intermediate goods during the reporting period. There were also fewer exports of machine, motor vehicle and ICT goods,

No further rise in exports recently

however. This contrasted with a moderate growth in exports of consumer goods.

Subdued import activity

Imports lost momentum entirely in the fourth quarter of 2011 in response to the slowdown in output and demand. Seasonally adjusted imports of goods showed a perceptible fall on the quarter in real terms. Demand for intermediate goods and energy showed the largest decline. Imports of consumer goods also slowed somewhat following a comparatively sharp rise in the preceding quarter. By contrast, imports of capital goods showed a further increase. Imports from the euro area as well as many Asian countries, including China, were trending downwards recently. On the other hand, US manufacturers were selling distinctly more goods in Germany again following the decline in the third quarter.

■ Sectoral trends

High level of industrial output in the third quarter not matched overall, ...

As expected, the fourth quarter saw a lull in the industrial upswing. Industrial output in the final three months of 2011 was a seasonally adjusted 2¼% down on its high level of the third quarter. This reflects the fact that the flow of orders was waning from mid-2011 onwards. The quite sharp decline in the reporting period was also due in part to a technical counter-movement in response to output which had been stepped up sharply in some segments of industry during the holiday months as a result of special measures. Given declining demand, the holiday quotas “saved” in the summer were increasingly being used up towards the end of the year. This is suggested by the fact that, in December, the number of hours worked per person employed in industry was a seasonally adjusted 2% down on the monthly average for 2011, while there was a noticeable peak in working hours in July. This “holiday effect” is also likely to be one reason why there was such an obvious fall in industrial output in December.

Underlying trends in foreign trade

Seasonally adjusted, quarterly



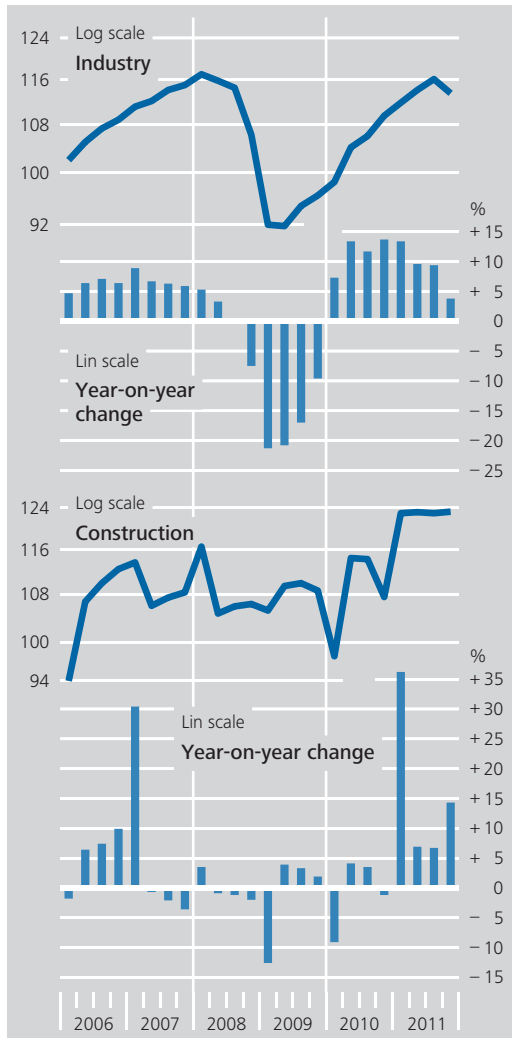
¹ Adjusted for the price indices for foreign trade.
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Production of intermediate and capital goods fell by 2½% in seasonally adjusted terms in the reporting quarter. The increase in the output of capital goods was significantly larger than this in the preceding quarter, however, so that output between October and December – in contrast to the intermediate goods sector – was still up on the level of the second quarter. This is consistent with the overall economic picture of a temporary lull in growth insofar as revisions to investment plans have tended to be minor, whereas purchases of inputs have been cut back perceptibly in order to save storage costs. Consumer goods output fell by a season-

... but capital goods output up on Q2

Output in industry and in construction

2005 = 100, seasonally adjusted, quarterly



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ally adjusted 1¼% in the reporting period, as in the preceding quarter.

Further decline in capacity utilisation at the start of the year

According to Ifo Institute data, manufacturing firms rated their capacity utilisation at the turn of 2011-12 somewhat lower again than in the preceding October. With utilisation at 84½% of normal full capacity, the January figure for industry was nevertheless still somewhat above the multi-year average. In the intermediate goods industry, capacity utilisation at the current end is estimated to be 83¼%, while the figure for the capital goods sector is 87½%. This gap is due to the generally higher utilisation in the case of capital goods. There is no

identifiable difference in the degree of utilisation relative to the respective sectoral average.

Seasonally adjusted construction output was only ¼% up on the quarter in the autumn months. Building construction went up ¾% in the reporting period following an increase of ¼% in the preceding three-month period. By contrast, there was a noticeable decline in civil engineering with a further fall of -¾%. Building construction's growth lead over civil engineering reflects the fact that the situation in housing and commercial construction is significantly better than in public sector construction at present. For the construction sector as a whole – leaving aside seasonal fluctuations due to the weather – an unchanged high degree of utilisation continues to be reported. Energy production in autumn was a seasonally adjusted ½% up on the quarter. There was a considerable year-on-year shortfall owing to the decommissioning of nuclear power plants: the minus figure widened again perceptibly to -10% after -8¼% in the second and third quarters of 2011.

Construction and energy output somewhat higher

While many services industries are unlikely to have felt the direct effects of the slowdown in industrial activity, the wholesale sector was unable to avoid this. The activities of transport and logistics enterprises were probably also impaired. For example, the mileage of domestic heavy goods vehicles on roads subject to toll charges declined by 1% in seasonally adjusted terms in the fourth quarter compared with the summer months. The statistics show a real decline in sales among retailers, too, at the end of the period under review. Motor vehicle traders experienced a slight increase in activity, however. Many craft trades were still benefiting from the positive construction activity and consumers' propensity to purchase.

Many services industries less affected by the slowdown in demand

Employment and labour market

Notwithstanding the cyclical slowdown, the labour market in Germany remains on an expan-

Continued growth in employment ...

sonary course. There was a marked rise in employment in the final quarter of 2011. According to the estimates of the Federal Statistical Office, the quarter-on-quarter increase, at a seasonally adjusted 129,000 persons in work in Germany (+0.3%), was roughly as high as in summer. The development in employment subject to social security contributions was again somewhat better than in employment overall. By contrast, there was a further decline in the number of government-assisted work opportunities (one-euro workfare jobs) as well as those solely in marginal employment. In seasonally adjusted terms, there was an increase in self-employment.

... mainly owing to additional jobs subject to social security contributions

In the first two months of the last quarter, employment subject to social security contributions increased by 135,000, or 0.5%, in seasonally adjusted terms compared with the average of the third quarter. The largest gains were in business-related services (excluding temporary employment) as well as in the health and education services. There was also substantial growth in the number of jobs in trade, the transport and logistics sector, the information and communications technology industry as well as in hotels and restaurants. It is striking that – unlike the situation just a few years ago – greater use was not made of atypical employment relationships in these sectors. Even so, these newly created jobs are likely to have involved part-time employment subject to social security contributions to a certain extent. The rise in manufacturing employment was slightly below-average. Among the sectors showing no job growth recently were the public authorities along with temporary employment, construction and education.

Rising immigration and employment numbers of persons from EU 8 countries

The growth in employment was accompanied by increased immigration of persons from the eight central and east European member states (EU 8) for whom complete freedom of movement has applied since May 2011. At 56,000 persons net between May and August 2011 alone – more recent Federal Statistical Office data are unavailable at present – more

than twice as many immigrants came from these countries to Germany than in the comparable period of 2010.² According to the Federal Employment Agency, employment subject to social security contributions of persons from the EU 8 countries increased by 47,000 in the four months up to August 2011, while there was merely a rise of 7,000 in the same period one year earlier. Part of the growth in employment was accounted for by persons who were already living in Germany before May 2011, however. For the following three months up to November 2011, the Federal Employment Agency is assuming a further increase of around 15,000 in the number of employees subject to social security contributions from the “accession eight” countries.

The net migration gains are not due solely to the effects of granting complete freedom of movement to workers who are nationals of these countries. According to an initial estimate by the Federal Statistical Office, Germany’s migration balance in 2011, at +240,000, was higher than at any time since 2001. The main reason for increased immigration is likely to be the favourable economic and labour market situation in Germany in relation to other European countries. Despite restrictions on freedom of movement that are still in force, more persons from Romania and Bulgaria came to Germany in the first eight months of 2011 than in the year before. Roughly one-tenth of net immigration came from Greece, Italy, Spain and Portugal. One year earlier, the migration balances with these countries were more or less level.

Migration balance clearly positive

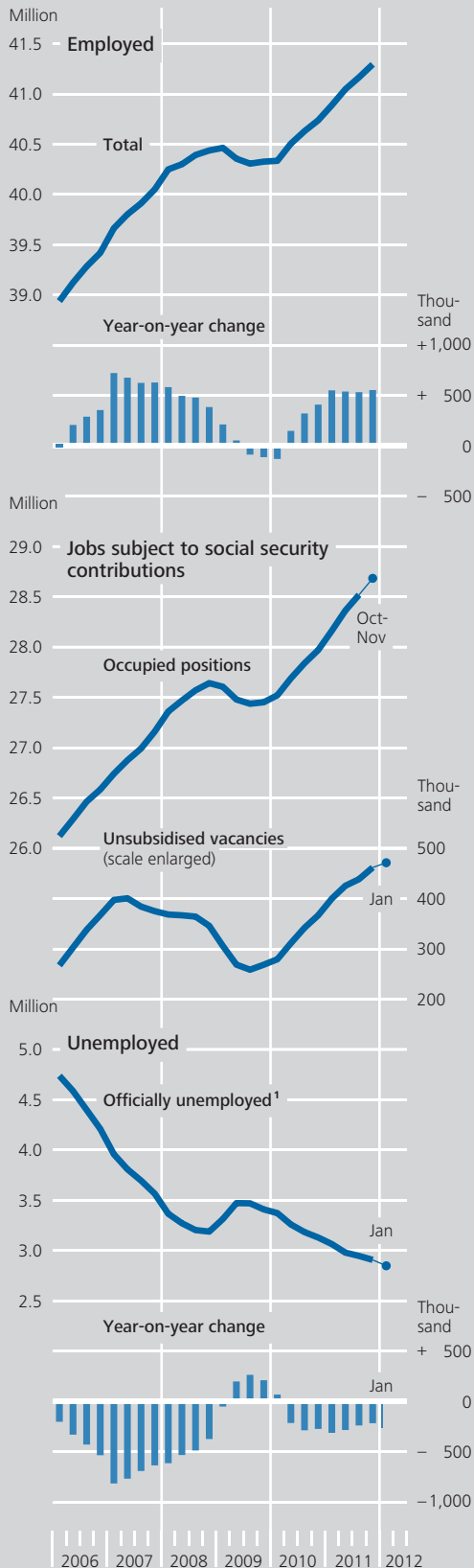
Recruiting employees abroad appears still to be a secondary option for most enterprises. According to the 2011 Labour Market Report of the Association of German Chambers of Industry and Commerce (DIHK), in terms of prevent-

Reports of shortages in qualified staff

² The provisional data of the Central Register of Foreigners show a net inflow of only 34,000 persons from the EU 8 countries for the eight months from May to December 2011 and thus probably understate immigration from this region.

Labour market

Seasonally adjusted, quarterly



¹ From May 2009, unemployed excluding persons newly registered on the books of private employment agencies.
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ing the emergence of shortages in qualified staff, preference is given to measures such as the targeted personnel development of young employees, increasing opportunities for vocational education and training, and the expansion of employment of older members of the workforce. Although, according to this survey, one enterprise in three reports difficulties in filling vacancies, this cannot be equated with a broadly based lack of specialised labour. Nor does it pose acute economic risks. According to the Ifo business survey, around one in ten manufacturing firms at present feels handicapped by shortages in the supply of labour. Irrespective of the current situation, the demographic outlook means that enterprises and the social partners are faced with the task of developing and implementing strategies in good time to prevent a future shortage of qualified staff.

There was a further reduction in unemployment in the fourth quarter. At a seasonally adjusted 2.91 million, there were around 39,000 fewer persons registered as unemployed than in the third quarter. The unemployment rate fell by 0.1 percentage point to 6.9%. As in previous quarters, there was a relatively steady decline in unemployment among those receiving basic welfare benefits (SGB II). Furthermore, there was a discernible reduction (15,000) again in unemployment among persons claiming insurance benefits (SGB III) after the decline had almost come to a standstill in the third quarter. Owing to the continued scaling-back of work opportunities in the additional cost variant (one-euro workfare jobs) and other active labour market policy measures, overall underemployment fell considerably more sharply on the year (-499,000) than registered unemployment (-216,000). In January 2012, there was a further marked fall in the official unemployment figure of 34,000. The unemployment rate fell to 6.7%.

Decline in official unemployment among both those receiving basic welfare allowance and persons claiming insurance benefits

The available leading indicators show that a continuing positive development may be expected on the labour market. As before, the

Continued positive outlook for the labour market

majority of enterprises are planning to increase staffing levels. The Ifo employment barometer, which measures the planned staffing levels for trade and industry over the next three months, shows a stable level for January compared with the average of the fourth quarter of 2011 after the index had been declining from its record high in the first quarter of last year. The fourth quarter saw a further sharp seasonally adjusted increase in the number of unassisted vacancies reported to the Federal Employment Agency. The BA-X job index, which is calculated on the basis of the level and intake of vacancies, showed a marked rise. Unlike in the last two quarters, both inflows and outflows of vacancies increased again somewhat, which suggests that the dynamics of the labour market are accelerating again. However, there was also a further considerable increase in the average time reported jobs remained vacant.

■ Wages and prices

Sharp rise in actual earnings in 2011, ...

The positive economic situation was clearly reflected in employees' earnings. Last year, gross wages and salaries per employee, at 3.4%, rose more sharply than at any time since 1993. One reason for this was higher collective wage agreements with higher scheduled increases in rates of pay. Another was that employers made – in some cases considerable – bonus and extraordinary payments on a voluntary basis. This was true, above all, of large industrial enterprises, which allowed their workforces to share in the success of their business. The normalisation of regular working hours and the increase in paid overtime also had the effect of boosting wages. For the current year, a shift towards higher negotiated wage increases along with a reduced wage drift appears likely. This is not due solely to the fact that pay agreements which have already been concluded are increasingly taking effect. An additional factor is that increases in remuneration are likely to be a key focus of the negotiations in this year's pay round, which covers a number of key industries. In this context, it will be necessary to

Negotiated rates of pay

Year-on-year percentage change, on monthly basis



¹ Excluding additional benefits and lump-sum payments.

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make an accurate assessment of the existing economic risks.

The moderate trend acceleration in negotiated basic rates of pay continued in the fourth quarter. According to the Bundesbank's statistics, they rose by 2.1% on the year in the final quarter of 2011, compared with 2.0% in the third quarter.³ Including all one-off payments and ancillary agreements, the rise in negotiated earnings in 2011, at 1.7% on an annual average, was only marginally higher than in 2010 (1.6%). One factor in this was that hardly any payment settlements were agreed in major sectors of the economy after mid-2011.

... but growth in negotiated rates of pay still moderate

The rate of price increase was tending to accelerate in the final quarter of 2011. Opposing forces were in play on the external side. On the one hand, commodity prices were being depressed by the global economic slowdown. Importers of intermediate goods benefited most from this. At the same time, the euro depreciated noticeably. This led to a clear rise again in the prices of energy imports. There was a sharp rise in the prices of consumer goods, too. Upward price pressure on imports of capital goods

Increase in import prices

³ The Federal Statistical Office, whose index excludes civil servants, reports an increase of 2.1% for the negotiated rates of basic pay in the fourth quarter, compared with 1.8% in the third quarter.

House prices in 2011 in Germany

House prices in Germany rose sharply in 2011. The rate of price increase – calculated on the basis of data provided by BulwienGesa AG for 125 towns and cities – was 5½%, a figure considerably higher than in 2010, which already recorded a perceptible increase of 2½%. For the first time since the reunification boom in the early 1990s, a cyclical upturn was accompanied in Germany by a marked price reaction on the housing markets. In comparison with the situation in other European countries, the German property market still occupies a special position, albeit with largely reversed price trends compared with the time prior to the financial and economic crisis.

With regard to Germany as a whole, the upward trend in property prices is likely to be somewhat overstated owing to the provisional nature of the data provided. This is due to the fact that the momentum is focused on urban regions, ie those areas where the price information of BulwienGesa AG over the reporting year is concentrated at present.¹ This, however, does not qualify the underlying trend of a marked acceleration in prices, especially as this is essentially confirmed by the other available indicators. According to the price index of the Association of German Pfandbrief Banks (*Verband deutscher Pfandbriefbanken, vdp*) for owner-occupied housing, house prices rose by 2½% in 2011, compared with just ½% in the year before. Hypoport AG's composite index shows that prices of new and existing owner-occupied apartments as well as single-family and two-family houses went up by 3½% in the reporting period, having increased by 2% in 2010. Looking at the annual average, the obvious upward trend, which has been a feature of the intra-year movement of these indicators since at least mid-2010, is reflected only to a limited extent. The differences in the individual results are, however, also due, in part, to statistical inaccuracies stemming mainly from the variations in recording by region and type of dwelling as well as to differences in the way in which the data are compiled.²

Rising house prices are to be seen in connection with the strong economic upturn, which was accompanied by a further improvement in the labour market situation and brought perceptible income gains to households. However, an even more significant factor in long-term decisions, such as whether to buy a property, is likely to have been that households' confidence with regard to employment and income prospects has not been affected by the current economic slowdown. Furthermore, households were still able to take up mortgage loans at extremely low rates of interest in 2011. In the fourth quarter of 2011, banks were charging an average of 3.6% on loans for real estate purchases with maturities of between five and ten years, which again matched the all-time low of the previous year following the somewhat less favourable interest rate conditions in the interim. Nevertheless, the development in prices meant that residential property did become slightly less affordable. Even so, surveys show that there was hardly any tightening of lending conditions during the year.

The pick-up in demand on the housing markets quickly led to perceptible price and quantity reactions as there has been a decline in the overall availability of housing over the past decade owing to very weak housing construction activity.³ The marked trend reversal in new construc-

¹ Initial calculations on the basis of a significantly broadened regional dataset provided by BulwienGesa AG, which, however, only goes as far as 2010 at present, show weaker price developments – measured against the benchmark – than in the comparable period of the previous year. The main reason for this is that house prices in rural areas have not increased as strongly as in urban areas. The broadly based house price index of the Federal Statistical Office, which does not provide data beyond the reporting year 2010 at present either, also indicates more moderate dynamics for Germany as a whole. See J Dechent, *Preisindizes für Wohnimmobilien*, Wirtschaft und Statistik, November 2011, pp 1126-1134.

² See also, for example, the information on property prices contained in the Bundesbank's Monthly Reports of February 2009 (pp 52-53) and February 2010 (pp 58-59).

³ See also Deutsche Bundesbank, *Extended investment cycle with stable prices: supply and demand in the German housing market from a longer-term perspective*, Monthly Report, June 2010, pp 47-58.

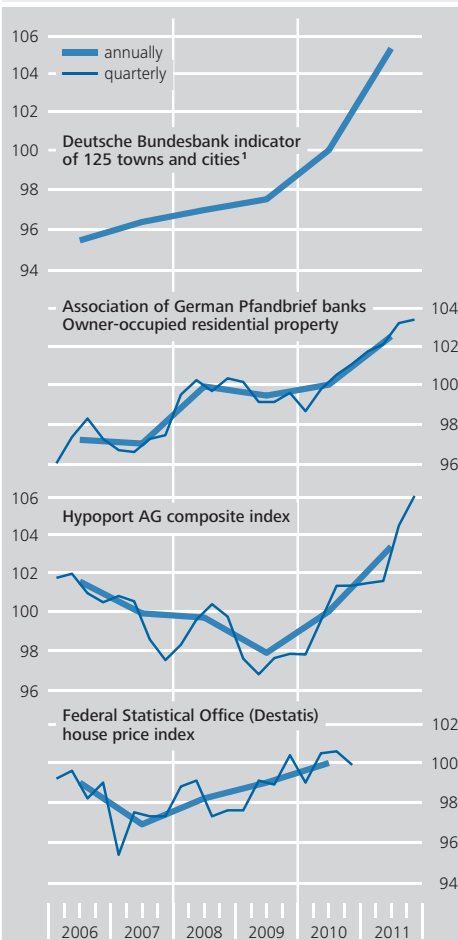
tion activity since 2010 is not just further evidence of the fact that demand has increased significantly in the intervening period; it also suggests that price pressure would have been even greater if supply had been less elastic. According to the provisional figures of the Federal Statistical Office, real housing investment went up by just under 6% in 2011. Building permits – measured in terms of the estimated costs for newly constructed housing – rose approximately by more than one-fifth on the volume of 2010.

The upward trend in prices now appears to have reached the German housing market on a broad front. The highest growth rates in 2011 – as in the previous year – were seen in larger towns and cities and their surrounding areas.⁴ This reflects the attractiveness of urban agglomerations, which are generally the first to benefit from an economic recovery. With regard to the price dynamics, the geographical location no longer plays a significant role, whereas differences in levels remain considerable. With regard to house price inflation differentials, convergence movements cannot be ruled out, especially between the large towns and cities. On these comparatively transparent markets, compensating forces may have tended to become a more significant factor owing to the heightened presence of investors. The fact that capital investment decisions are again having a greater impact in shaping the housing market in Germany is also apparent in the thriving demand for apartments in multiple-family dwellings. Despite extensive housing construction activity, demand has been outstripping supply considerably for some time now. This market situation led to a 7% rise in the price of new apartments in 2011, after marked price inflation at 4% in 2010. The increase in resale prices was only marginally lower.

The brighter outlook for the German economy in terms of structural growth tends to justify the fact that optimism has increasingly returned to the German housing market, too. Nevertheless, it should be borne in mind that, from a longer-term perspective, demand for housing will essentially be determined by the relatively unfavourable demographic benchmark figures, which themselves can be influenced only to a

Selected house price indices

2010 = 100, log scale



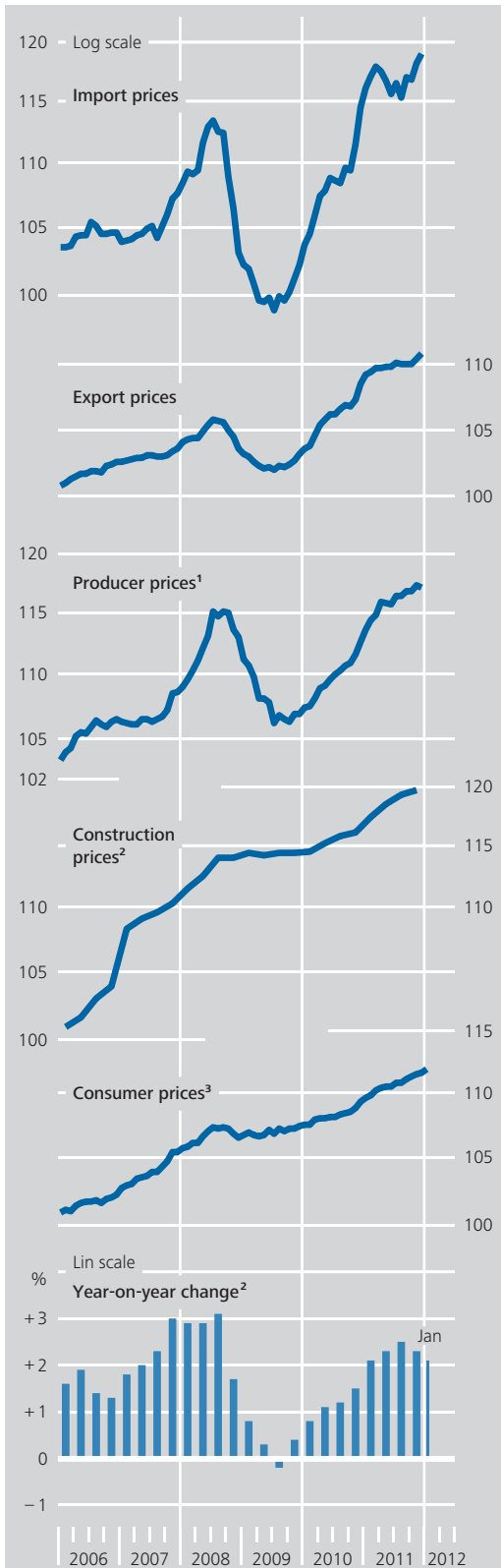
¹ Bundesbank calculations for semi-detached houses and owner-occupied apartments based on data provided by BulwienGesa AG.
 Deutsche Bundesbank

limited extent by the emerging increase in migration. This also places a limit on the potential of macroeconomic growth. There is thus no guarantee that the prospective available scope for expenditure for housing purposes can be broadened to the extent that rising purchase prices can always be covered by rental income. The potential for a setback in prices is still manageable, however. This risk should be faced, however, especially in the case of investment in residential property with the aim of safeguarding real value.

⁴ In larger towns and cities (around 500,000 inhabitants or more), prices for semi-detached houses and owner-occupied apartments rose by 7% in 2011, compared with 3¼% in 2010.

Import, export, producer and consumer prices

2005 = 100, seasonally adjusted, monthly



1 Producer price index for industrial products in domestic sales. **2** Not seasonally adjusted, quarterly. **3** National consumer price index.

accelerated. Even so, the overall year-on-year rate of increase in import prices fell to 5.5%, since the sharp rise in crude oil prices one year earlier is no longer taken into consideration.

In the fourth quarter, German industry was able to push through price increases in domestic and export sales on a scale similar to those in the third quarter, namely by ½% on average. The annual rate for producer prices fell to 4.8% and for export prices to 2.7%. The weaker valuation of the euro in the forex markets was accompanied by a deterioration in the terms of trade.

Construction prices continued to accelerate in the wake of robust construction activity. The year-on-year figure remained largely unchanged at nearly 3.1%. According to the calculations of the Association of German Pfandbrief Banks (*Verband deutscher Pfandbriefbanken*), purchase prices for owner-occupied housing were 0.2% up on the third quarter and 2.3% higher than in the same period of 2010 (see pages 50-51 for details of house prices in 2011).

Consumer inflation was marked by the sharp rise in energy prices as a result of the depreciation of the euro. If energy is excluded, the rate of price increase fell on the quarter, however, with the abolition of student tuition fees in North Rhine-Westphalia in October being a factor. Added to this were accelerated price reductions in the case of clothing and shoes, probably on account of the mild weather conditions. If these special effects are subtracted, a gradual acceleration of inflation is evident in the underlying trend. Including energy, consumer prices rose, at a seasonally adjusted 0.5%, somewhat more sharply on a quarterly average than in the preceding period. The annual CPI figure was unchanged at 2.4% and HICP inflation was 2.7%. Over the quarter, however, the annual CPI rate of inflation fell from 2.6% in September to 2.1% in December and the HICP figure went down from 2.9% to 2.3%.

... and in industrial sales prices

Rising construction and real estate prices

Gradual easing of consumer inflation

Consumer prices rose sharply at the beginning of 2012 at a seasonally adjusted 0.3%. Petroleum products became clearly more expensive again owing to higher crude oil prices, the impact of which was reinforced by the depreciation of the euro. Furthermore, the prices of shoes and clothing were now reduced less sharply than usual. Services became markedly more expensive. Rents, too, were trending upwards. The annual CPI and HICP figures remained unchanged at 2.1% and 2.3% respectively. The year-on-year rate is likely to go up again in February before possibly easing again in the following months as the energy and food price shocks of early 2011 gradually drop out of the calculations.

■ Orders received and outlook

Brighter outlook for growth

There was a perceptible improvement in the outlook for the German economy towards the end of the reporting period. In the first quarter of 2012, external retarding factors will weigh on production again. From spring onwards, the cyclical drivers of growth could gain the upper hand, however. A fairly rapid resumption of growth, which was the assumption underlying the December projection, now looks more likely. In a setting of somewhat calmer financial markets, enterprises are gaining new confidence, while domestic demand remains on a sound expansionary course. According to the Ifo surveys, business expectations in trade and industry have made a clear recovery from their interim low in the autumn months.⁴

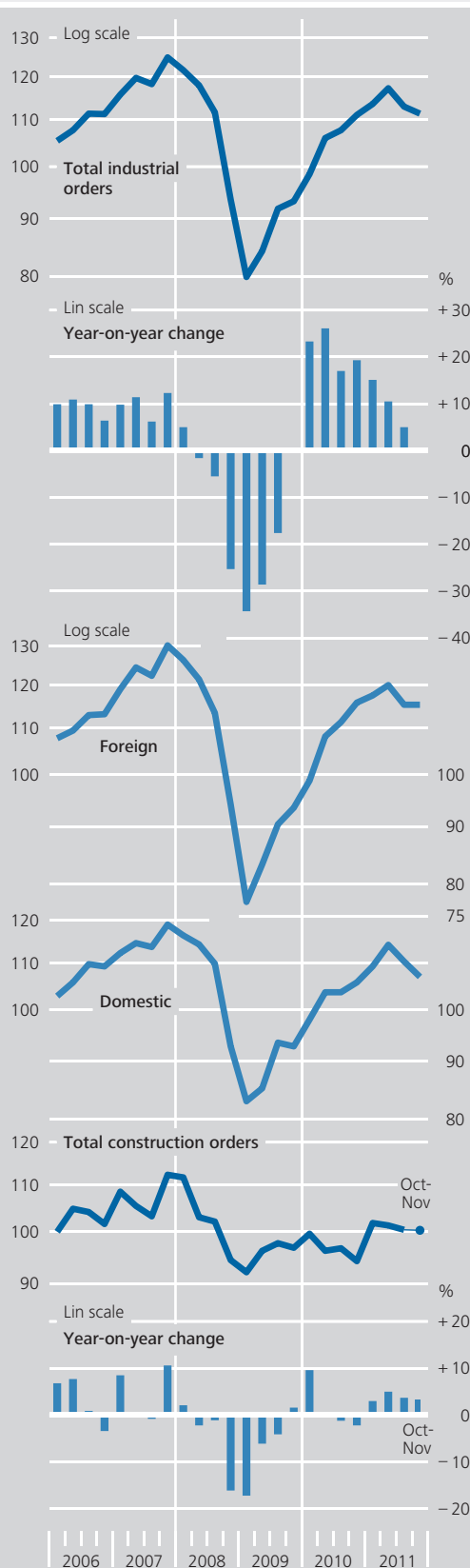
More industrial orders again from non-euro-area countries

In industry, assessments of the business situation were likewise tending to point upwards slightly towards the end of the period under

⁴ The latest DIHK survey from the beginning of 2012 shows that business expectations have deteriorated slightly since the preceding survey that took place between the end of August and the end of September 2011. This does not contradict the finding of the monthly Ifo business survey, however. First, the more pessimistic assessments in the former case date essentially to the period following the last DIHK survey. Second, new economic signals tend to show up in the DIHK survey with a certain time lag compared with the Ifo business survey.

Demand for industrial goods and construction work

Volume, 2005 = 100, seasonally adjusted, quarterly



review. Seasonally adjusted incoming orders, however, were easing off again in the fourth quarter. The quarter-on-quarter decline, at 1½%, was only half as strong as in the third quarter, although it should be borne in mind that the sharp fall in the third quarter was due to the volume of large orders returning to normal after the decidedly large volume in spring. Leaving aside the manufacture of other transport equipment, orders of which were very heavily influenced by this, the reduction in goods orders during the reporting period, at a seasonally adjusted 2%, was, in fact, larger than in the preceding quarter (-¾%). The flow of orders from non-euro-area countries turned positive. Orders from this region between October and December were 4% up on the quarter in seasonally adjusted terms. By contrast, there was a further (3%) fall in domestic orders and orders from non-euro-area countries slumped by as much as 5½%.

Orders of inputs still on the decline, but growth in capital goods orders

The sharp fall in demand for inputs in the fourth quarter suggests that the first few months of 2012 will also be marked by the dip in growth. Orders of intermediate goods were pointing upwards again in seasonally adjusted terms, however, even if weak demand from the euro area meant that the increase was no more than subdued. Machinery and vehicles made in Germany were nevertheless in heavy demand again from non-euro-area countries. Consumer goods demand in autumn 2011 was slightly down on the quarter overall, with domestic business being the decisive factor. The no more than moderate ½ percentage point decline in manufacturing capacity utilisation between October and January suggests, in line with output expectations, that industrial production will decline less sharply in the first quarter of 2012 than it did towards the end of 2011.

Buoyant construction demand will give strong stimuli to the economy for the foreseeable fu-

ture. This also applies to the winter months, unless weather conditions result in production being interrupted for prolonged periods. In that case, significant catching-up effects could be expected in spring, however. While civil engineering will probably tend to weaken owing to declining public sector demand, a period of high utilisation lies ahead for building construction. The orders situation in this segment is decidedly favourable at present, not least because it is being underpinned equally by housing construction and commercial construction. Measured by the estimated construction costs, the past three years have seen an underlying trend increase in building permits for housing construction. In October and November 2011, the volume was a seasonally adjusted 1¾% up on the average of the preceding quarter. There was a surge in commercial construction during the same period. Despite generally high volatility and the comparatively significant impact of major projects, it is notable that October and November saw commercial office buildings being approved on a scale that exceeded the average volume of the first nine months of 2011 by more than one-quarter. The expansion in demand for commercial construction has been broadly based for some time now. It has been especially strong in factory buildings, however, while growth in newly approved office and administrative buildings has been more subdued.

Private consumption will continue to buoy economic activity. The ongoing positive sentiment among consumers is the key factor in this respect. As they see it, income risks exist only on a limited scale at present. As a result, savings motive are receding in importance, particularly as deposit rates are currently extremely low. Not only do households feel that the time has come to purchase large durable goods, they are also probably spending more on recreation, leisure and entertainment.

Construction demand strongly expansionary

Upward trend in private consumption