

## Economic conditions in Germany

### Underlying trends

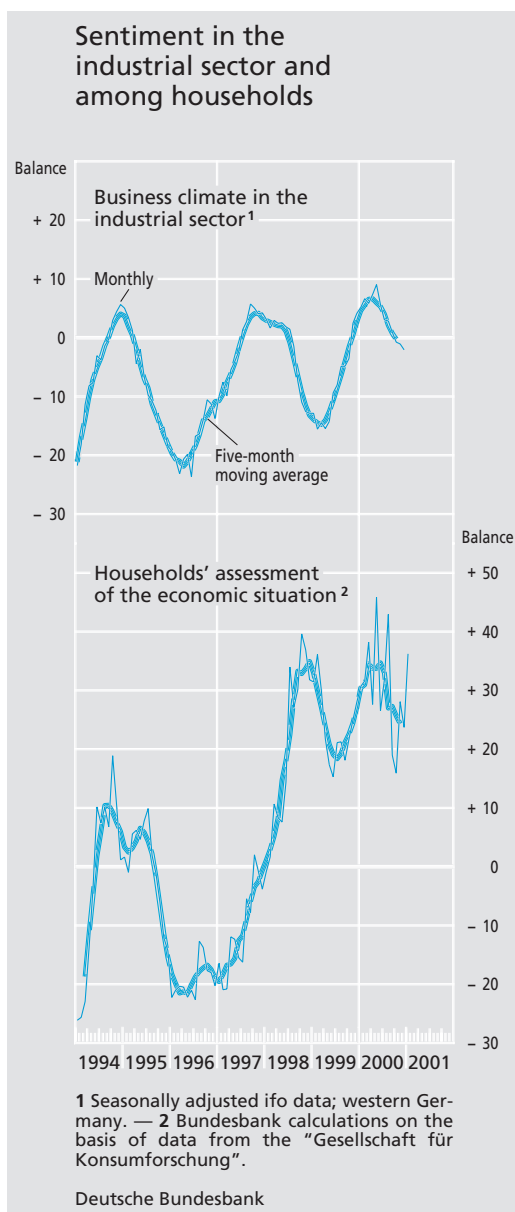
---

The German economy raised its output further in the last few months of 2000, and the improvement on the labour market continued. Following a period of sharp growth, the underlying pace of economic activity was much slower, however. On an annualised basis, the rate of expansion in the first six months of 2000 had amounted to 3¾%, compared with 2½% in the second half of the year. According to the Bundesbank's own calculations, the increase in real gross domestic product (GDP) in the fourth quarter of 2000, which had been influenced by comparatively strong calendar effects as well as by favourable weather conditions, may have gone down to ¼%. At the end of the period under review, the expansion of overall economic output was therefore probably lagging behind the concurrent increase in production capacity. Adjusted for variations in the number of working days, growth was nearly 2¾% up on the corresponding period in 1999; in calendar-month terms the figure was roughly 2%.

*GDP in Q4  
2000*

A major role in the slackening of economic activity was played by the fact that oil-price-induced strains were having a stronger impact. This affected households' real incomes as much as it did enterprises' profitability. Furthermore, uncertainties – especially about the US economy, which had long been playing the role of an engine of global growth – are likely to have depressed sentiment. According to the surveys of the ifo institute, for example, positive assessments in the business community have subsided noticeably of late,

*Oil-price-  
induced strains  
and higher risks*



with negative ratings gaining the upper hand. In the case of commercial service providers, which had previously been performing well, the slowdown in industry and the still incomplete process of structural adjustment in the construction sector were having an adverse impact.

Nevertheless, business sentiment could be more pessimistic at the moment than is dir-

ectly warranted by the economic data. Oil prices have generally been on the decline, and the strains which had arisen earlier are becoming less severe. At the same time, a gradual calming of inflationary pressures is apparent. The improvement in the terms of trade and the relief afforded by tax reform are likely to impart major stimuli to households' propensity to consume. The terms of financing in the longer-term maturity categories, which are more important than interest rates at the short end of the market, also remained favourable. They continue to provide a sound basis for an economic upswing. Moreover, enterprises' price competitiveness – which had been improving well into the final quarter of 2000 – was still high, even with a higher exchange rate for the euro. There are thus good prospects that the current slowdown in growth will not become entrenched and that the underlying tendency of economic activity will be maintained.

*The outlook remains positive*

### Output and labour market

Industrial output in the autumn of last year did not quite match that of the third quarter, which had shown a further significant increase on what, for some time, had already been a sharp upward trend in growth. Seasonally adjusted output in the period from October to December was ¼% down on the preceding three-month period. The fact that the level of output remained high despite this slight fall is revealed not least by a year-on-year comparison; as in the third quarter, the level in the fourth quarter was up nearly 8% on the year. According to ifo institute data,

*Declining industrial output*

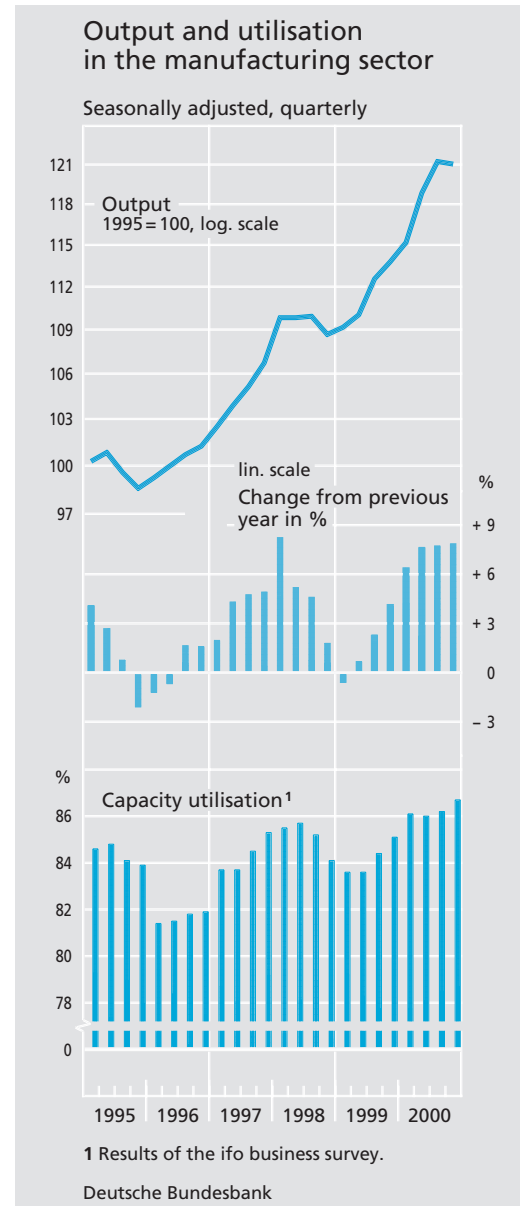
the level of capacity utilisation remained well above average in autumn.

Output in consumer-related industries was reduced comparatively sharply. This mainly affected the durable goods sector, where automobile production, in particular, was down on the high level of the summer months. Producers of non-durable goods also had cause to make cutbacks, however. Especially in the clothing and shoe industry, developments have for some time now been much less favourable than in 1999. Even so, the year-on-year rate of expansion in output in the capital goods sector, which likewise recorded losses, remained in double figures up to the end of the period under review. In particular, production of telecommunications equipment remained unchanged at a very high level.

*Weather conditions favourable to construction*

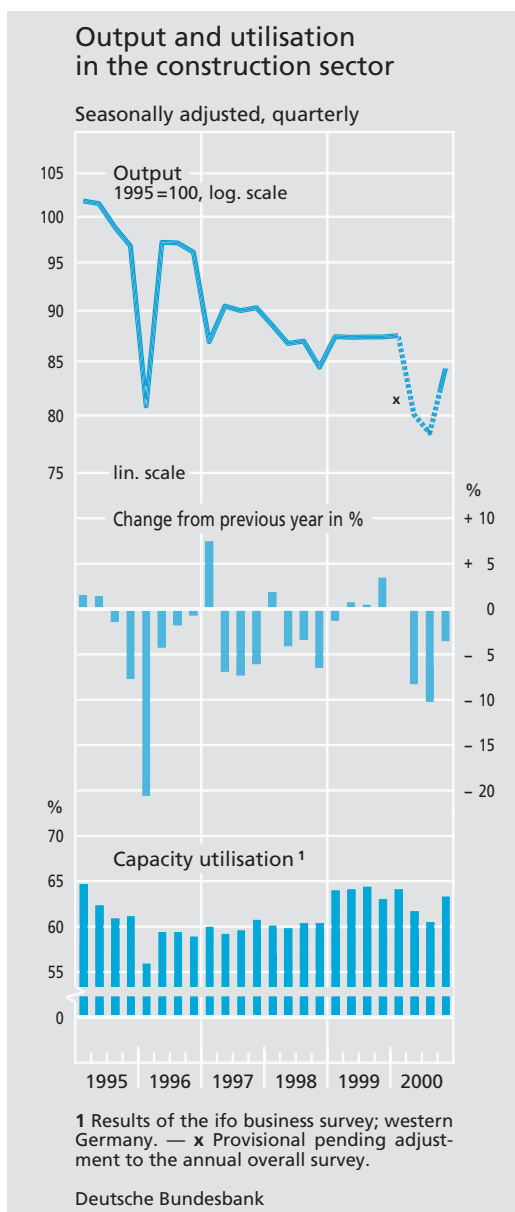
Construction sector output benefited considerably from the mild weather conditions in the last few months of 2000. According to the data of the ifo institute, only a small number of firms complained of restrictions due to the weather. After adjustment for seasonal variations, construction activity in the autumn months was comparatively buoyant. The preceding year-on-year decline in output was largely made good, although the improvement in the situation which this shows is likely to be only temporary. The unfavourable situation as a whole will re-emerge quite soon, particularly since it may be assumed that site work was largely suspended due to the cold snap in January 2001.

Developments on the labour market remained positive in autumn 2000. Employ-



ment rose again sharply, and there was a steady reduction in unemployment. According to Federal Statistical Office data, the seasonally adjusted number of persons in work increased to 38.69 million in November. This was roughly 140,000 more than around the middle of last year and 550,000, or 1.4%, more than 12 months previously. The mild weather probably played a part in fewer persons in outdoor occupations being laid off

*Sustained improvement on the labour market*



than is usual at this time of the year. Yet again, commercial and private service providers achieved the sharpest increases in staffing levels. However, wholesale and retail trade, hotel and restaurant services and industry likewise probably hired more workers. By contrast, in the construction sector the balance of recruitment vis-à-vis lay-offs remained negative.

The number of persons registered as unemployed with the Federal Labour Office showed a marked decline by the end of 2000. In December, the seasonally adjusted number of registered persons amounted to 3.77 million, i.e. roughly 130,000 fewer than in mid-2000 and 240,000 fewer than in December 1999. The unemployment rate, which had been as high as 9.6% in seasonally adjusted terms at the end of June, fell to 9.2% at the end of the year. In January 2001, there was a slight seasonally adjusted rise in unemployment, since work in the weather-dependent outdoor occupations had been hampered more than before by the onset of winter weather.

*Falling unemployment*

As has been the case for some while, the trend improvement in the labour market situation applies only to western Germany, where the unemployment rate fell from 7.7% in the middle of 2000 to 7.3% at the end of the period under review. In eastern Germany, however, the rate in December and January, at 17.2%, was not only much higher but was also nearly unchanged from mid-year.

The easing effect of labour market policy measures at the turn of 2000–2001 did not quite match the high level achieved previously. The number of persons attending vocational training courses in December and January, at an average of 365,000, was somewhat higher than in the summer and represented a year-on-year increase of slightly more than 35,000. At the same time, however, the number of persons working on job creation schemes fell to just under 285,000, which

was a fall of nearly 70,000 compared with 1999. By far the largest part of that figure is accounted for by the new Länder, which benefited only to a below-average extent from the expansion of vocational training.

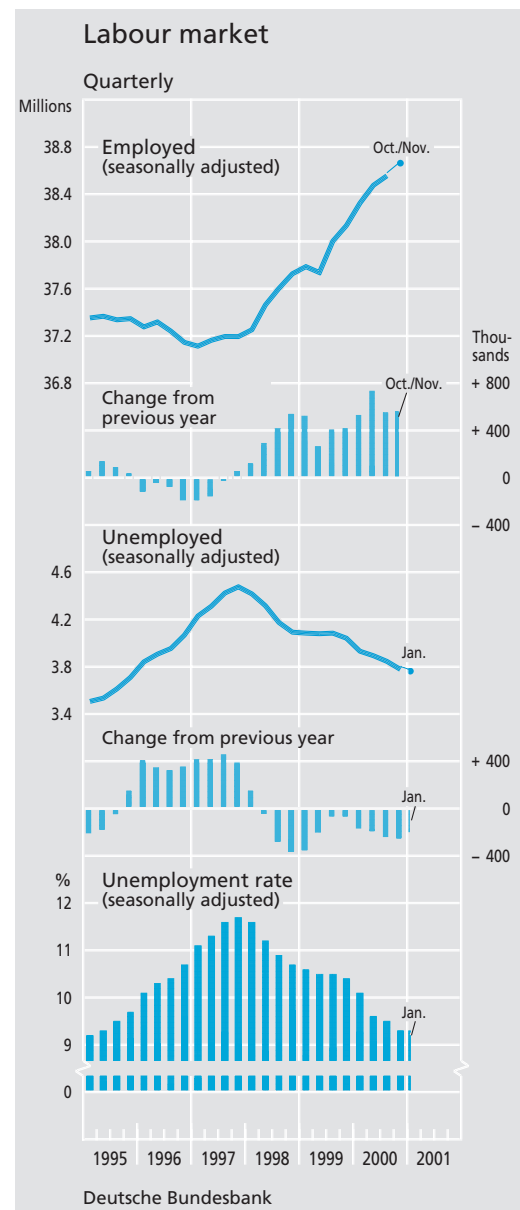
## Orders

### *Improvement in manufacturing order books*

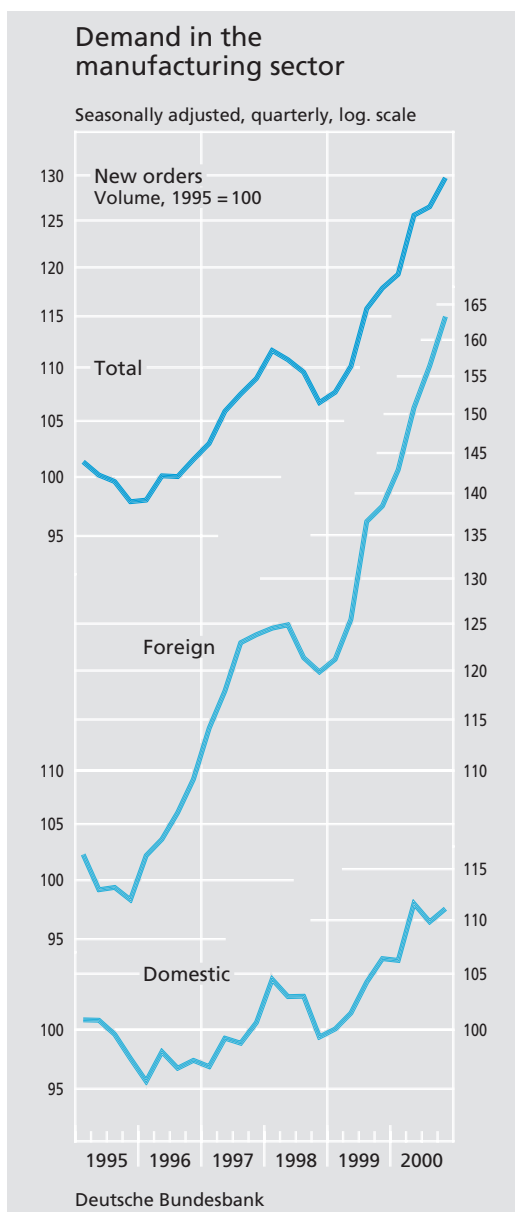
There was a further improvement in manufacturing order books in autumn 2000. Seasonally adjusted, orders received by the manufacturing sector in the fourth quarter were 2 ½ % higher than in the preceding three-month period. The year-on-year increase, which had amounted to around 9 % in the third quarter, went up to just over 10 %.

Yet again, foreign customers placed a large volume of new orders. After adjustment for seasonal variations, orders in the final quarter of the year were almost 4 ½ % higher than in the summer. At around 18 %, the year-on-year rise was, in fact, larger than in the third quarter. By contrast, incoming domestic orders towards the end of the year were, in seasonally adjusted terms, only slightly up on their level in the preceding months. The year-on-year rate of increase fell back from 5 ½ % to 4 ½ %.

For producers of capital goods, in particular, the year-on-year increase in demand was sharper than average, with double-digit rates of growth being achieved in the fourth quarter as well. The top position was occupied by producers of telecommunications equipment and makers of precision instruments. There was also perceptible growth in the manufac-



ture of other transport equipment, which includes shipbuilding and aircraft manufacturing. Against that, there was a slackening of the pace of growth in ordering for intermediate consumption, which had been very brisk as recently as the summer. Even so, ordering was still more buoyant than in the case of producers of durable and non-durable goods, among which the furniture industry and



clothing manufacturers performed comparatively poorly.

Many of the orders received over the past few months were large-scale contracts. Judging by past experience, only some of these orders are reflected in production during the reporting period, however. A considerable number of them will have been put on the order books and will be processed only grad-

ually. At present, the capital goods sector, in particular, has a large stock of orders on hand. This will benefit output over the next few months and will ensure a steadier utilisation of capacity.

Orders received by the construction sector in October and November 2000 were – seasonally adjusted – around 1 % higher than in the preceding summer months. Whether this means that demand for construction work has stabilised has to remain an open question at present, however. Even at the end of the period under review, the level of orders was roughly 8 ¼ % down on the year.

*Stabilisation of construction orders*

The public sector, in particular, placed more orders for construction work towards the end of last year. In the first two months of autumn, the seasonally adjusted volume of new orders was roughly 3 ¾ % higher than in the preceding three-month period. The year-on-year fall, which had been in double figures in the summer, was reduced to 3 ½ %. Additionally, the industrial sector also stepped up its construction activity somewhat. Seasonally adjusted, orders in October and November were just over 1 % up on the preceding quarter. This was still clearly (i. e. 7 ¼ %) down on the figure for the same period in 1999, however.

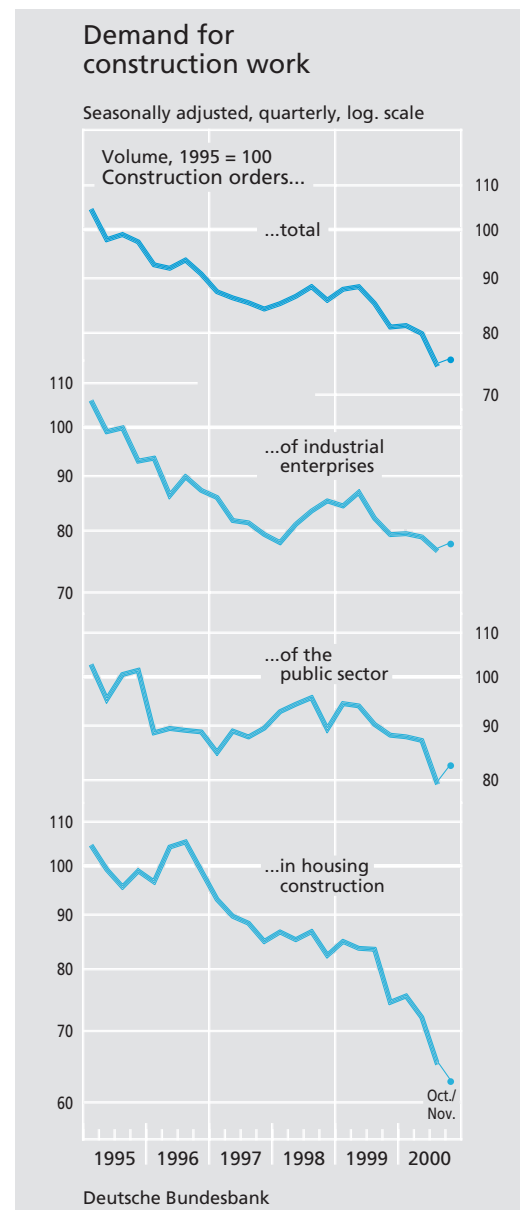
In contrast to the above-mentioned construction subsectors, the situation in housing construction at the end of last year continued to deteriorate. In seasonally adjusted terms, the (already low) level of business activity fell by another 3 ¾ % in October and November, and was 17 % down over 12 months. The de-

cline was even sharper in eastern Germany, where orders were now only at two-fifths of their level in 1995. This is partly due to the fact that there are still numerous vacant properties in eastern Germany that cannot be let. In western Germany the situation is somewhat more favourable to the extent that the level of new orders agreed with the construction firms in the final quarter of the year was no lower than it had been in the summer months. This was still a significant (around 13%) year-on-year fall, however, even though it was no longer as large as it had been in the third quarter (-18%). Taking construction permits as a yardstick, there is still no sign of a change for the better. Rather, the seasonally adjusted number of construction permits for both single and two-family housing and for rented accommodation, in particular, showed a further fall compared with the already low figures in the summer. In all cases, the figures continued to be roughly one-quarter down on the year.

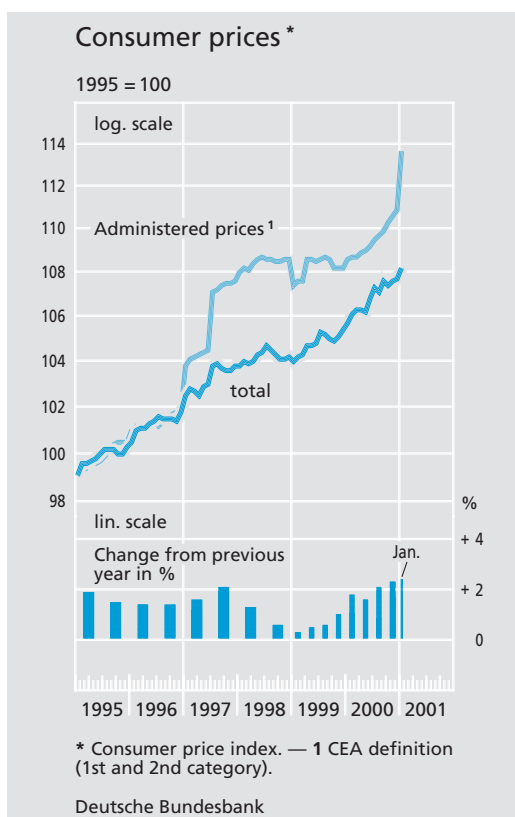
## Prices

*Strong influence of administered prices*

The year-on-year rate of increase in consumer prices, which had declined to 2.2% at the end of 2000, went back up again in January. At 2.4%, it was again approaching its level of September, which had witnessed the sharpest rise in 2000. This renewed acceleration was mainly due to a number of administrative measures which came into effect at the start of 2001. For example, a perceptible increase in motor vehicle tax came into force for older vehicles which do not fully meet the stringent requirements relating to exhaust



emissions. According to the calculations of the Federal Statistical Office, this resulted in an average increase of just under 30%. Added to this was a significant increase in radio and television licence fees (from DM 28.25 to DM 31.45 a month). Finally, there was the impact of the third stage of the ecological tax reform, which raised the price of petrol by 6 pfennigs per litre and made electricity 0.5 pfennig more expensive per



kilowatt hour. In purely mathematical terms, these three factors increased the cost of living by roughly  $\frac{1}{2}$  percentage point compared with the previous month.

In terms of food products, prices for seasonal goods such as fruit and vegetables, in particular, have risen quite sharply as a result of the cold weather in January. In the case of meat and fish, the BSE crisis led to price movements in the opposite direction. Whereas fresh beef and processed beef products became cheaper, rising demand meant that, on balance, fresh and processed pork and fish products became more expensive. Overall, food cost 2.2 % more in January 2001 than twelve months before, compared with 1.4 % in December 2000.

The fact that the price increase for energy at the start of 2001 was comparatively limited is due solely to mineral oil products. The price reductions on the international oil markets have been a factor clearly offsetting tax increases and persistent price adjustments in the case of gas and contributions to the cost of central and district heating. Both were raised again in January owing to the time lag vis-à-vis heating oil prices in working their way through to the consumer.

At 0.5 %, the year-on-year rate of price increase for industrial goods, in particular, remained far below average. Housing rents rose by 1.3 % in January and services (excluding radio and television licence fees and motor vehicle tax) were 1.5 % more expensive than at the start of 2000.

The Harmonised Index of Consumer Prices (HICP) used by the ECB gives a year-on-year rate of price increase of 2.2 % in January, compared with 2.3 % in December. The discrepancy between this index and the consumer price index produced by the Federal Statistical Office is due to the fact that motor vehicle taxes are not included in the HICP.

Measured in terms of US dollar prices for Brent Oil, international oil prices during January were going back up again compared with their low level at the turn of 2000–2001. Even so, on a monthly average they remained slightly down on the corresponding figure for December. This meant that, for the first time in more than 20 months, oil was hardly any more expensive than it had been 12 months previously. Even though there was a slight

*Fall in international oil prices*



year-on-year rise when calculated in Deutsche Mark, the appreciation of the euro has eased the situation over the past few weeks. The rise in prices on the international oil markets accelerated again in the first two weeks of February, however.

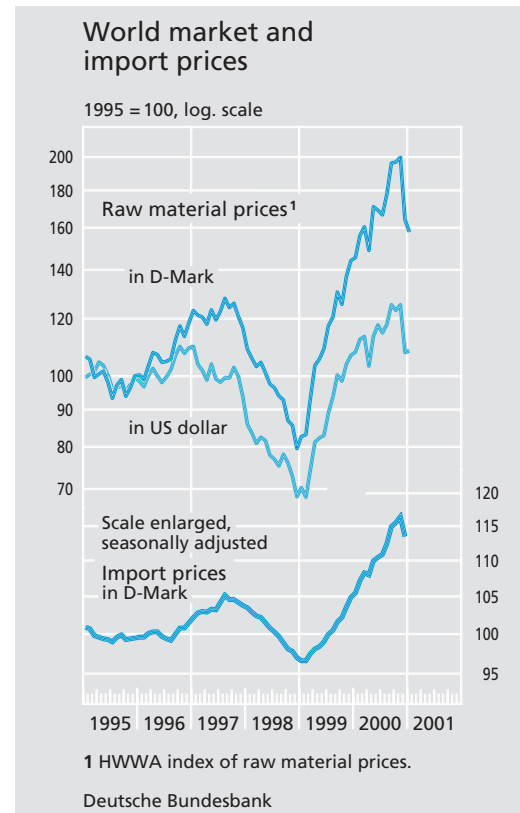
*Imports have become less expensive*

In December 2000 (more recent data are unavailable at present), German import prices fell sharply in seasonally adjusted terms. The year-on-year rate of increase, which had been as much as +12.5% in November, went down to +8.2%. The main reason for this was a marked fall in prices for crude oil and mineral oil products, more than offsetting the further rise in the price of gas. Added to this were exchange-rate-induced price reductions in the case of imports of non-energy raw materials.

On the other hand, the appreciation of the euro meant that exporters lowered their selling prices. As this reduction was significantly less than the easing with regard to imported goods, however, there was a marked improvement in the terms of trade for the first time in two years. The year-on-year decline therefore went down to 4.5%, compared with 7.4% in the previous month.

*Diverging industrial producer prices*

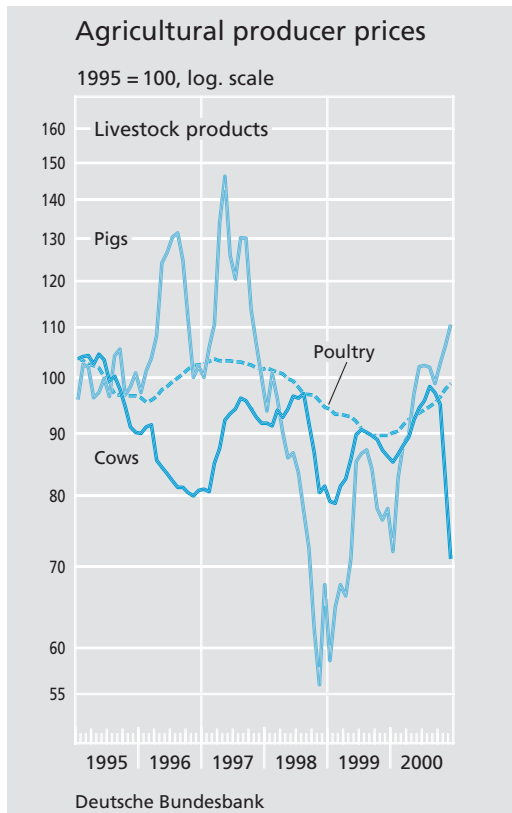
The inflationary pressures of industry on domestic sales in December have eased up as well, in seasonally adjusted terms. The year-on-year price increase went down to 4.2%, compared with 4.7% in November – due solely to the fall in oil prices. Excluding energy, the year-on-year rate of increase continued to rise slightly – from 2.2% to 2.4% in December. The pace of inflation over 12



months has accelerated in the case of both capital and non-durable goods.

After adjustment for seasonal variations, there was a sharp fall in agricultural prices in December, following a long period in which there had been a trend rise. The rate of year-on-year increase, having peaked at 10% in October, was 7.0% at the end of the period under review. Firstly, prices for fruit and vegetables did not go up as much as one year before. Secondly, in the case of livestock products, the decline in prices for cattle due to BSE were much sharper than the price increases for poultry and pigs, which benefited from a substitution-induced rise in demand accompanied by a cyclical recovery of prices on the pig markets.

*Slower rise in agricultural producer prices*



There were still only minor price movements in the construction sector during the last few months of 2000. Seasonally adjusted construction prices went up by no more than 0.3% compared with the third quarter. As before, this was 0.8% more than in the same period in 1999. The rise in prices for road building continued to be far higher than average owing to the fact that increases in the cost of oil-dependent intermediate consumption have a stronger impact. By contrast, there was a comparatively slight increase in the residential construction sector. At the end of the period under review, shell construction work was also 0.7% cheaper than 12 months previously.

*Construction prices largely stable*